

PROPORTIONALITY IN INTERNATIONAL INVESTMENT LAW

Are we there yet?



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1 Introduction

1.1 Proportionality as a standard of review in international investment law

Arbitration tribunals do from time to time find themselves confronted with situations under which they are obliged to balance competing juridical positions, be they norms, interests or values. A fundamental issue is thus how such balancing operations should be undertaken. A range of methods, otherwise known as “standards of review”, have both been proposed and is utilized in practice. One particular alternative is known as “proportionality”. This thesis aims to assess to what extent proportionality is, and should be, preferred as the applicable standard of review within the field of law known as international investment law. The latter currently exhibits a somewhat confused state of affairs regarding this issue, a situation that is becoming more and more intolerable as the economical importance of international investment law continues to accelerate.

Over the last 25 years the amount of inflation adjusted world foreign direct investment (FDI) inflow has increased by approximately a factor of 35, to a staggering 1.7 trillion US dollars in 2008.¹ During the same time span, inflation adjusted world GDP has only increased by a factor of slightly below 6.² The economical importance of investments across international borderlines is thus on the rise, both in absolute and relative terms.

With increased economical importance follows increased juridical significance. From being a field of relatively light regulatory pressure, international investment law has shown a remarkable development over the recent decades. Highlights include the rise of bilateral investment treaties (BITs) from a number of about 400 in 1991 to 2676 at the end of 2008,³ as well as a surge in arbitral proceedings related to the subject area.⁴ Also, this field of

¹ See UNCTAD Beyond 20/20 FDI Statistics.

² See the IMF World Economic Outlook database.

³ See the UNCTAD World Investment Report 2009.

⁴ As an illuminating example of this assertion, the International Centre for Settlement of Investment Disputes

study has increasingly been on the agenda of both commentators and practitioners within the international juridical community.

Even so, the sources of law governing international investments still exhibit a somewhat murky relationship. Municipal legislation, so-called investment contracts, customary international law, and treaties of both bilateral and multilateral character regularly clash in a contest without clearly defined rules of the game. In short; the legal structure regulating any single relationship between an investor and the foreign state in which his investment is located is currently quite polyphased and generally somewhat inconclusive.

Within such a frame of reference, this paper will, as indicated, mainly deal with proportionality as a standard of review in the context of international investment law. The overreaching question tried answered is to what extent it presently applies within the sphere of this legal subject. As a standard of review alternative possibly employed by an investment tribunal in its scrutiny of the claim at issue, proportionality may influence the procedure of the court and, through it, the outcome of the case. The question is thus of importance both in terms of legal theory, and in terms of factual consequences for anyone contemplating an international investment claim.

1.2 Initial definitions

Having already utilized a number of key words and expressions, this section will seek to define them more clearly, as well as introduce some additional terminological concepts of fundamental importance. To start off with the basics, the term “foreign investment” refers, in principle, to an asset owned by an entity (called the investor) located in another country than that of the asset (called the host state). “International investment law” denotes the general body of law governing such bilateral ventures. In practise, a lot of controversy surrounds both the question of what constitutes an asset, the question of what constitutes an

(ICSID) had in 2009 more than twice as many cases as in 2000 and 8 times as many as in 1995 according to its Caseload Statistics.

investor and the question of location of both the investor and the asset.⁵ Thus, a universally accepted definition of “foreign investment” is so far lacking, with the predictable legal consequences. There exist a lot of definitions out there of more limited applicability though. Article 1 of the US Model BIT of 2004 provides, for instance, an illustrative example of such a denotation, valid within the Model BIT’s sphere of reference.

A quantity of more concrete proportions is the BIT. The phrase connotes a treaty between two states at the level of public international law which aims to set standards of protection for (or convey rights to) the investors of the one country with assets within the other. As such, they are typically ‘designed to cover the following five substantive areas: (i) definition of investment and investor; (ii) admission of foreign investors; (iii) fair and equitable treatment of investors; (iv) compensation in the event of expropriation; and (v) methods of settling disputes’⁶.

An instrument not dissimilar to the BIT is the multilateral investment treaty (MIT). It is in essence a BIT between more states than two. In this thesis, the term will be used for both multilateral treaties open to any state, and multilateral treaties of a more sectorial or regional character. As of 2010 there are few MITs in existence despite several attempts to create a common set of foreign investment rules of global validity.⁷ The most well known are perhaps chapter 11 of the North American Free Trade Agreement (NAFTA) between the North American states, and the Energy Charter Treaty (ETC) with its strict sectorial scope.

The (potential) host state may also undertake to negotiate a so-called “investment contract” directly with the investor. The aim of such a device would be similar to that of the BIT and MIT in pegging down some standards of investment protection, but in this instance that protection would be based on a contractual relationship between the host state and the investor rather than on a treaty valid through public international law. As shall be discussed in section 2.2.2, the exact nature and legal significance of investment contracts

⁵ See section 2.4 for a more thorough discussion of this topic.

⁶ Subedi, S. P., *International Investment Law: Reconciling Policy and Principle*, chapter 4 page 84.

⁷ See Schill, S. W., *The Multilateralization of International Investment Law* chapter II section E as well as section 2.2.3 of this thesis.

may be disputed.

Finally, the term “proportionality” refers to a method for resolving apparent conflicts between differing legal norms, principles and values through a three-step trade-off procedure. It is often referred to as a legal principle,⁸ providing, as shall be more thoroughly examined in chapter 3, a standard against which competing juridical quantities can be measured and equated. It should perhaps be stressed at this point that proportionality as a concept is in no way unique to international investment law. Indeed, it currently enjoys a far stronger foundation in other fields of law than it does here.⁹ This thesis’ topic is a function of proportionality’s emerging, though not yet completely clarified, position within the boundaries of international investment law.

Additional words and expressions will be identified and defined where and when they are needed.

1.3 Delimitations and clarifications

The scope of this thesis encompasses the utilization of standards of review (in particular proportionality) in the context of international investment law. Though other juridical subjects will be mined for illustrative material, it therefore, in principle, limits itself to an analysis with applicability but within this cited legal discipline. Furthermore, standards of review are (as shall be seen) concerned with the juridical process rather than with its results and effects. Thus, the forthcoming argumentation will not handle any issues of enforcement and continuation (etc.), for instance damage calculations, even though the standards of review it discusses may be seen to have an impact on such matters.

Another crucial distinction that the argumentation of this thesis rests upon is the line between a question of standard of review and a question of what is known as intensity of

⁸ See for instance Andenæs, M. and Zleptnig, S., *Proportionality: WTO Law in Comparative Perspective* chapter II section A part 1.

⁹ Proportionality is for example presently a dominant feature of the law emerging from the European Convention on Human Rights (ECHR), and its importance is also on the rise in both international trade law and EU law among other disciplines. See generally section 3.2.

review or margin of appreciation. While the former question relates to how a tribunal should conduct a certain juridical process (the method), the latter is basically a matter of how strictly the chosen standard of review should be applied relative to the autonomy of the parties to the dispute (the actual application of the method).¹⁰ As shall be seen, both commentators and practitioners often jumble the two questions together, and thereby cause unnecessary juridical confusion. While it acknowledges that there exist a certain interrelation and mutual influence, this thesis will argue that standard of review and intensity of review are separate concepts best reviewed separately. In tune with its scope, it will subsequently proceed to address the former and only refer to the latter where clarity and consistency so demands.

Finally, the argumentation of this thesis shall also be delimited against the concept commonly known as burden of proof. Though there are links between the burden of proof imposed on the parties and the standard of review employed by the tribunal, the discussions below are thus limited to an assessment of the latter. The reason behind this demarcation is similar to the one concerning intensity of review in that while standard of review issues concern a juridical process, burden of proof relates to the application of that process. The two concepts are thus essentially separate entities that for the sake of clarity should be reviewed separately.

1.4 Structure of the thesis

The thesis starts off with an overview of international investment law (chapter 2) intended to introduce the main concepts, sources of law and operative methodology of the subject. Readers already familiar with the topic may consider skipping the chapter altogether. Note though that the main discussions of chapter 5 are based on the terminology and approach developed in chapter 2, some of which tackles issues currently considered juridically controversial. It may for that reason be prudent to have read the chapter in order to be able to adequately grasp the basis of the subsequent argumentation.

Chapter 3 introduces and develops the concept of proportionality as well as indicates

¹⁰ This distinction will be further clarified in section 3.1.4.

its current general diffusion throughout international and municipal law. As shall be established, proportionality is a standard of review, or procedural framework, utilizable in situations where two or more competing juridical norms, interests and values need to be equated. Again, readers already familiar with the concept may consider skipping the chapter. Since both commentators and practitioners of differing legal backgrounds do seem to differ slightly as to their initial understanding of proportionality however,¹¹ it is advisable that at least section 3.3 is scanned.

Trying to dodge the pitfalls of an overly theoretical discussion, the argumentation of chapter 5 will utilize a constructed investment case as a backdrop. Chapter 4 outlines this case scenario between the fictional entities known as the RDA and Xanadu, as well as clarifies the topic of the thesis in terms of practical applicability and relevance. The chapter also presents a number of assumptions formulated to sharpen the focus of the subsequent discussion.

Chapter 5 contains the main discussion of the thesis in evaluating proportionality's diffusion and utility within international investment law at the end of 2010. Several different fields of applicability are identified (based mostly on the fictional investment case outlined in chapter 4) and assessed.

Finally, chapter 6 is intended to gather any loose ends and provide a conclusion of sorts. It shall be shown that though proportionality by no means is cemented in international investment law as of today, trends seem to be pulling the standard towards increased utility and importance. It will also be argued that proportionality may be considered good practice in face of the impending issues international investment law probably will revolve around in the forthcoming years.

¹¹ See section 3.2.

2 Foreign investments and international investment law

This chapter is intended as a short introduction to international investment law per se. First, it will outline the field of study by way of some general remarks (section 2.1). Second, the sources of law encountered therein will be subject to a brief scrutiny on the basis of the historical development of the discipline (section 2.2). Third, the methodology that later shall be relied upon, will, to a certain extent, be sketched out (section 2.3). Finally, as a starting point for the subsequent discourse, the fundamental though somewhat controversial question of what constitutes an investment will be highlighted (section 2.4). The latter topic is structurally included among these initial notes because a basic grasp of its content is required in order to discern the principal discussion that this thesis primarily concerns itself with. It should perhaps too be noted that the wide perspective of this chapter to some extent might cause it to foreshadow argumentation further developed later. In such eventualities, reference is made to the passage where the argument is examined in more detail.

2.1 A brief overview of the field of study

The basic model of international investment law comprises legal restrictions on host state sovereignty in order to attract foreign investments.¹² Whether or not the implied postulate of this model holds true, whereupon a legal system more restricting on state sovereignty will attract more investments, is, however, a matter of some debate that will not be further addressed in this thesis.¹³ The essential point to be noted is instead that international investment law fundamentally concerns itself with granting the investor rights he otherwise not would have enjoyed under mere municipal law. The juridical cause for

¹² See Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter I section 3.

¹³ For an in-depth study of the topic, see Sauvant, K. P. (ed.) and Sachs, L. E. (ed.), *The Effect of Treaties on Foreign Direct Investment*.

such an arrangement lies, as section 2.2 below will touch upon, in the international character of the investor-state relation.

Investments, as opposed to trade, are furthermore economical instruments of long time-horizons, often involving substantial financial value both for the investor and for the country in which the investment is to be located. Before the investment is made, the potential investor therefore often has a powerful bargaining position relative to that of the potential host state which he will use to secure as strong a legal protection for his investment as possible, insulating it from political risks.¹⁴ Subsequently however, the table is turned. Now the host state sits with the stronger cards through its monopoly on legislative power within its domain. At this point, the investor is in essence left with a lot of sunk costs that he hopes will yield profit over the investment time-horizon. In the case of an ensuing dispute between him and the host state, he must hence rely on the assumption that the legal protection he initially attained limits the state's potential expropriatory interests and/or legislative latitude.

At its core, international investment law is similar to other jurisprudence in primarily concerning itself with the settlement of legal disputes. An analytical challenge presented by this field of study though, is that 'it cannot be adequately rationalised as either a form of public international or private transnational dispute resolution'¹⁵, at the same time as it basically transverses the sphere of mere municipal law. Thus, neither national courts nor established international tribunals such as the ICJ are inherently equipped to deal with international investment cases. Such disputes therefore, have, to date, mainly been handled by specific investment tribunals, either established on ad hoc basis or through more permanent bodies such as the International Centre for Settlement of Investment Disputes (ICSID).

As for the investment projects themselves, frequently large and complex endeavours, they often affect many aspects of the society in which they are executed. In juridical terms,

¹⁴ A "political risks" being the risk of unwanted economical consequences of political activity, for instance the altering of contract law, expropriation of property or interference or prevention of business transactions. See generally Kobrin, S. J., *Political Risk: a Review and Reconsideration*.

¹⁵ Douglas, Z., *The Hybrid Foundations of Investment Treaty Arbitration*, chapter 1 page 152.

the rules of foreign investment thus often touch upon several facets of municipal law such as labour law, environmental law, law of property, and health law among other legal disciplines. This begs the question of what will happen in the event of a conflict of laws. May the host state do as it pleases with reference to national sovereignty, possibly eroding the investment protection of the investor, or is the latter anchored at an international level and therefore resistant to municipal legislature? That international investment law to a certain extent amounts to a body of international rules is fairly obvious,¹⁶ but the exact content and reach of these, as well as their relative impact, is contested. Thus, an essentially unresolved, though fundamental, question of preservation of national sovereignty in relation to democratic legitimacy underscores the very fabric of any juridical question herein circulated, highlighting the somewhat complex and unsettled nature of this subject.

In short; international investment law may be characterized as field of juridical study at the crossroads of public international law, international economic law and municipal law concerning investments. Additionally, a few distinct rules peculiar to its own sphere of jurisdiction have evolved throughout the recent decades. This academic province thus blurs the distinction not only between national and international law but also public and private law. The effects are a high degree of juridical complexity, but also the potential for flexibility.

2.2 The sources of international investment law

International investment law is a relatively new constellation in the juridical sky. Even though the foreign investment concept is far from any kind of recent innovation, a separate standard of protection for such assets has been juridically conceptualized in its present state only during the recent decades: Until after the First World War, investments owned by aliens were regulated in the same way as investments owned by the native inhabitants of the state; mainly through municipal law. So far, the international juridical community had been 'primarily concerned with allocating jurisdiction among States, as the only subjects of

¹⁶ See Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter I section 3.

international law'¹⁷. In the event of a dispute, an investor thus either had to initiate legal proceedings before the courts of the host state, or petition his own state for it to pursue his case against the host state at the level of public international law. The first mentioned alternative is of little desirability since the host state holds monopoly on legislative power through its territorial sovereignty,¹⁸ while to depend on the latter position is somewhat risky since there neither is any guarantee that public international law has any standards which may be relied upon in the particular case, nor is there any guarantee that the state of the investor is interested in picking up the case at all.¹⁹

Then came the twentieth century, and with it some historical events that set the wheels of international investment law turning. A taste of what would be came already in the *Lena Goldfields* arbitration of 1930 when an international tribunal awarded compensation to a private alien claimant against the Soviet Union after that nation had nationalized the claimant's property during the Russian revolution of 1917.²⁰ It was followed by a few other similar cases,²¹ but system did not properly kick into gear until the second half of the 20th century: The aftermath of World War II left private investors within the loosing states frustrated as they lost large bulks of their foreign property in negotiated settlements between their countries and the former Allies.²² This created political pressure for the development of a system that might lead to more secure and predictable multilateral investment conditions. At around the same time, the process of decolonization bore with it a taking of foreign property on behalf of the newly independent states.²³ Also the Eastern

¹⁷ Leal-Arcas, R., *The Multilateralization of International Investment Law* chapter III page 53.

¹⁸ See Brownlie, I., *Principles of Public International Law*, 7th Edition part III chapter 6.

¹⁹ There are nevertheless examples of investors choosing this path. See the ICJ *Diallo* case part III.

²⁰ For a review of the award, see Veeder, V., *The Lena Goldfields Arbitration: the Historical Roots of Three Ideas*.

²¹ Mostly between the US and its Latin American neighbours. Note in this context also the importance of the earlier so-called Calvo Doctrine formulated by the Argentinean Carlos Calvo. See generally Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter I pages 13-14.

²² See Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter I page 18.

²³ See Newcombe, A., and Paradell L., *Law and Practice of Investment Treaties* chapter 1 §1.14.

European, now communist, nations indulged in this practise.²⁴ Further political pressure for a more coherent system of international investment law was thus advanced by the (mostly Western) states of private capital outflow to better secure the assets of their subjects in the future. Also, technological advancement and liberalization of international financial markets led to easier transfer of capital,²⁵ making the investment world smaller and the investment flow greater. In total, several factors now jointly pushed for an accelerated development of more advanced regulation on foreign investments, better suited to handle the needs of the modern investment community.

The result was both polyphased and is still pending. Polyphased because several relevant and overlapping sources of law crystallized. Still pending because the interrelation between these have yet to be finally defined and resolved into a consistent body of international investment law. The different sources of law in question can be divided into the categories of bilateral treaty law, multilateral treaty law, investment contract law and customary law of international investment. Also, municipal law does to a certain extent, depending on the question at hand, influence the jumble. Some notes on each category here follow.

2.2.1 Customary law of international investment

The customary law of international investment is perhaps the more disputed of the categories both in terms of its relation to the others, and in terms of its content. It is regarded as a 'source of international law as it expresses an *opinio juris* within the international community that the principle involved has to be accepted as obligatory',²⁶. Traces of it can be glimpsed as far back as the middle of the twentieth century in the form of the international minimum standard of the treatment of aliens.²⁷ In short; the states were (and for that matter still are) bound by public international law to award foreigners within

²⁴ See Sornarajah, M., *The International Law on Foreign Investment*, 3rd edition chapter 1 pages 23-24.

²⁵ See Kelsey, J., *The Denationalization of Money: Embedded Neoliberalism and the Risks of Implosion*.

²⁶ Sornarajah, M., *The International Law on Foreign Investment*, 3rd edition chapter 2 page 82.

²⁷ See generally Roth, A. H., *The Minimum Standard of International Law Applied to Aliens*.

their jurisdiction a minimum of legal protection along several axes. One such axis covered their investments.²⁸ The exact content of these minimum standards is disputed, however. The dividing line of opinion has historically been (and to some extent may still be) traced between net capital exporting states seeking high levels of investment protection through internationally binding standards, and net capital importing states seeking to maintain as much state sovereignty as possible.²⁹ Some consensus seems never the less to have been reached in a UN Resolution of 1962 which holds that foreign investment agreements entered into by a state must be observed in good faith.³⁰ What a demand for “good faith” entails with regard to investment law is still not entirely clear though. Suffice it to say that, among other things, both principles of fair and equitable treatment³¹ principles of economic sovereignty of states³² and principles of compensation for expropriation³³ have, with mixed results, been advocated as customary international investment law based on a concept of good faith as a minimum standard of the treatment of aliens.

The UN General Assembly Resolution No. 3281, the Charter of Economic Rights and Duties of States, should hereunder be mentioned. This one was perhaps the culmination of the developing countries’ push for a “New International Economic Order”³⁴, and endeavoured to provide any host state with substantial juridical latitude against foreign investors by, among other things, asserting a principle of permanent state sovereignty over

²⁸ Some commentators seem to deny that there exist any customary law of international investments at all though. See for instance Trimble, P., *International Law and World Order* page 835.

²⁹ Sort of a culmination of this strife might have been the UN Resolution called the Charter of Economic Rights and Duties of States of 1974. See below for a brief discussion regarding this document.

³⁰ See the *UN General Assembly Resolution No. 1803* paragraph 8. To what extent a UN Resolution creates customary law as evidence of an *opinio juris* of the international community is a somewhat debated question that will not be addressed by this thesis. See Brownlie, I., *Principles of Public International Law, 7th Edition* part I chapter 1 section 3 and section 4 page 15.

³¹ See the NAFTA Free Trade Commission Note of Interpretation of the 31st of July 2001 on NAFTA article 1105(1) as well as McLachlan, C., *Investment Treaties and General International Law* part II section A.

³² See Castañeda, J., *The Underdeveloped Nations and the Development of International Law* page 39.

³³ See Ripinsky, S. with Williams, K., *Damages in International Investment Law* chapter 4 section 4.2.1(a).

³⁴ See generally White, R. C. A., *A New International Economic Order*.

natural resources.³⁵ The resolution did, however, not get the impact it was envisioned for several reasons that will not be delved deeper into here.³⁶ Arbitration practise has in general not taken much account of it either.³⁷

Related to customary law are general principles of law. The latter expression refers to rules accepted as evident by all civilized states.³⁸ As seen above also was the case with the customary law of international investments, arbitration practice contains several incidents of postulates being termed principles of international investment law based on the argument that they stem from general principles of law.³⁹ Some commentators argue that investment law principles founded in general principles of law are weaker sources of law than principles funded in customary law though.⁴⁰ The reasoning seems to be that the content of general principles of law often is somewhat diffuse and generally manipulative according to subjective preferences. Nevertheless, tribunals do continue to find and apply postulates of international investment law without discrimination as to the basis of their origin.⁴¹ As for ICSID tribunals, such practice would seem to be in tune with article 42 of the ICSID Convention, which states that, unless something else is agreed upon, the tribunal shall ‘apply [...] such rules of international law as may be applicable’. Also, article 31 of the Vienna Convention on the Law of Treaties refers to international law as a factor that generally should be taken into account when interpreting (investment) treaties.⁴²

³⁵ See the *UN General Assembly Resolution No.3281* ‘The Charter of Economic Rights and Duties of States’ article 2.

³⁶ See Yackee, J. W., *Pacta Sunt Servanda and State Promise to Foreign Investors Before Bilateral Investment Treaties: Myth and Reality* sections III and IV for a thorough discussion of the topic.

³⁷ See for instance the *Texaco v Libya* award paragraphs 23-24 and 29-31, which contains an illustrative discussion of the topic.

³⁸ See Brownlie, I., *Principles of Public International Law, 7th Edition* part I chapter 1 section 6.

³⁹ The standard of full compensation for the expropriation of foreign property is, for instance, based on notions of unjust enrichment and acquired rights as general principles of law. See *Factory at Chorzów: Award on Merits* page 47.

⁴⁰ See Sornarajah, M., *The International Law on Foreign Investment, 3rd edition* chapter 2 section 5.3.

⁴¹ Ibid. chapter 2 page 86.

⁴² See McLachlan, C., *Investment Treaties and General International Law* part I section C. The Vienna Convention will be further discussed in section 2.3 below.

2.2.2 *Investment contract law*

Since investment projects frequently stretch over long time spans, involve a lot of financial value and are comprised of complex legal interrelations, the investor and the host state often find it prudent to enter into contracts regulating the specific project at hand. In particular investments relating to the extraction of natural resources by foreign companies are often governed investment contracts; for instance so-called concession agreements within the field of oil and gas.⁴³ The great controversy regarding this source of law has been, and to some extent still is, the issue of whether, and to what extent, the state party is bound by such contracts when they (as they often do) delimit its territorial sovereignty.⁴⁴ Another way to put this is to ask whether the contracting parties may choose, with binding effect, that an investment contract is to govern their legal interrelation in case of a dispute (in other words an inquisition of choice of law). An affirmative answer to this question, without any qualifications, is often equated with the principle of *pacta sunt servanda*.⁴⁵ This one states in its pure form that ‘agreements and stipulations [...] must be observed’⁴⁶. Within the context of international investment law, theories of internationalization have, on the basis of a concept of *pacta sunt servanda* as a customary principle of law, been advocated to ensure a legal foundation for the binding nature of investment contracts, anchored at the level of international law.⁴⁷ Such contracts would hence be insulated from of the host state’s competence to unilaterally alter by changing the underlying municipal contract law. If governed solely by the latter, the host state would have such competence as a function of its territorial sovereignty.⁴⁸

It would seem that this so-called internationalization doctrine is both slightly

⁴³ See Bishop, R., D., *International Arbitration of Petroleum Disputes: The Development of a Lex Petrolea*.

⁴⁴ See Sornarajah, M., *The International Law on Foreign Investment*, 3rd edition chapter 7 introduction.

⁴⁵ See for instance *ARAMCO v Saudi Arabia* page 152, *Sapphire v NIOC* page 181 and *Aminoil v Kuwait* page 1023.

⁴⁶ Garner, B. A. (ed.), *Black’s Law Dictionary 9th Edition* on *Pacta sunt servanda*.

⁴⁷ See for instance Nougayrède, D., *Binding States: a Commentary on State Contracts and Investment Treaties* pages 375-376 as well as assertions in arbitration awards such as *Sapphire v NIOC* page 181 and *Texaco v Libya* paragraph 88 among others.

⁴⁸ See Brownlie, I., *Principles of Public International Law*, 7th Edition part III chapter 6.

controversial,⁴⁹ and perhaps also somewhat outdated, however.⁵⁰ This thesis will not further address or illuminate it. As for investment contract law otherwise, international law does not provide any coherent system regulating the field, thus causing tribunals faced with investment contract related issues to rely, at least partly, on other sources of international investment law, for instance on the relevant municipal legal system or on any BIT or MIT in effect.⁵¹ The specifics here too lie outside the scope of this thesis.

2.2.3 *Multilateral investment treaties*

Though several international initiatives have tried to establish one, no MIT of general scope exists in the world of today. A first effort of conjuration was undertaken already in 1929 by the League of Nations through its Draft Convention on the Treatment of Foreigners.⁵² It never made it. An international investment code was then tried included within the 1948 outline of the International Trade Organization, but that entity did not even get off the drawing board.⁵³ Then came and went a few more proposals,⁵⁴ before the

⁴⁹ For a fairly comprehensive review of the critique see Sornarajah, M., *The International Law on Foreign Investment*, 3rd edition chapter 7 section 2.

⁵⁰ Instead of internationalization based on a hard concept of *pacta sunt servanda*, it may be argued that contemporary jurisprudence rather favours a concept of protection of legitimate expectations and acquired rights. See Alvik, I., *Contracting with Sovereignty: State Contracts and International Arbitration* chapter 5 section 5.5. Alternatively, *pacta sunt servanda* may be understood as but a presumption against a unilateral termination of a promise. See Yackee, J. W., *Pacta Sunt Servanda and State Promise to Foreign Investors Before Bilateral Investment Treaties: Myth and Reality* section III part A.

⁵¹ In the words of the Permanent Court of International Justice (PCIJ) in the *Serbian Loans Case* page 41: '[A]ny contract which is not a contract between States in their capacity as subjects of international law is based on the municipal law of the same country'. See also Maniruzzaman, A. F. M., *Choice of Law in International Contracts – Some Fundamental Conflict of Laws Issues*, especially sections II and III.

⁵² See Van Harten, G., *Investment Treaty Arbitration and Public Law* page 19.

⁵³ See Hart, M., *A Multilateral Agreement on Foreign Direct Investment – Why Now?* page 52.

⁵⁴ Notably the Abs-Shawcross Draft Convention on Investments Abroad, the Draft Convention on the Protection of Foreign Property of the OECD, and the investment treaty initiative during the WTO Uruguay Round of the GATT.

Organization for Economic Co-operation and Development (OECD) in 1996 launched negotiations for the Multilateral Agreement on Investment (MAI).⁵⁵ Though being a fairly ambitious treaty project of some prestige, the MAI too failed to see the light of day however, due to a number of reasons that will not be delved deeper into here.⁵⁶ Subsequently, the push for a MIT of general scope seems to have deflated somewhat despite negotiation on the topic within the World Trade Organization (WTO) Doha Round at the 2003 Cancun summit.⁵⁷ At the moment, a new effort of conjuration does not seem eminent.

There exist, nevertheless, some MITs of more limited scope out there: In a regional context, chapter 11 of the NAFTA has provided foreign investment protection between the North American states since 1992, and the Association of Southeast Asian Nations (ASEAN) encompasses both a Treaty on the Protection and Promotion of Foreign Investment and a Framework Agreement on Investments.⁵⁸ In a sectorial context, the ECT of 1994 furthermore contains provisions for protection of investments in the energy sector of Europe.⁵⁹ Last but not least, the ICSID Convention on the Settlement of Disputes between States and Nationals of Other States establishes a multilateral framework of elective procedural rules for conducting investment arbitrations between investors and host states party to the convention. This one has been in place since 1965, and is closely tied to the World Bank.⁶⁰ Its scope is, however, entirely voluntary as state ratification of it does not provide direct substantive rights to foreign investors. Rather, it provides a binding framework for arbitration if both parties to an investor-state dispute agree to utilize its

⁵⁵ See Schill, S. W., *The Multilateralization of International Investment Law* chapter II section E.

⁵⁶ A lot of ink has been invested in documenting the rise and fall of the MAI. See for instance Muchlinski, P. T., *The Rise and Fall of the Multilateral Agreement on Investment: Where Now?*.

⁵⁷ See Wallace, C. D., *The Legal Environment for a Multilateral Framework on Investment and the Potential Role of the WTO*.

⁵⁸ See Sornarajah, M., *Protection of Foreign Investment in the Asia-Pacific Economic Co-operation Region*.

⁵⁹ See Waelde, T., *International Energy Law: An Introduction to Modern Concepts, Context, Policy and Players*.

⁶⁰ See Schill, S. W., *The Multilateralization of International Investment Law* chapter II section D subsection 1.

prospect.⁶¹ Thus the ICSID Convention, though having an unmistakable impact on international investment law of today,⁶² cannot be characterized as a MIT in the true meaning of the expression.

2.2.4 *Bilateral investment treaties*

The rise and rise of the BITs may very well be viewed as a direct consequence of the failure of the international community to produce a MIT of general scope: 1962 saw the dawn of a new era in international investment law as the very first BIT, between Germany and Pakistan, entered into force.⁶³ From there on their number increased slowly to about 308 at the end of 1988, before it exploded during the 1990s and onward.⁶⁴ As of today the BIT complex constitutes a grid between most nations of the world, similar perhaps to sort of a nervous system of international investment law: To a certain extent, BITs are interconnected through both their relative conformity, and the so-called Most Favoured Nation (MFN) clauses prominent in most contemporary investment treaties.⁶⁵ These provide that the protection of investor rights guaranteed under a certain BIT should be at least as far-reaching as the protection enjoyed by investors under all other BITs that the host state is party to.⁶⁶ Thereby, the network of treaty relationships plugged into through the contracting of a single BIT may have more sweeping consequences for a nation than initially foreseen.

Viewed at the aggregate level, the global effect of the BIT complex is not unlike that of a MIT. Some argue that the developing countries, together a prominent force behind the collapse of most of the MIT-initiatives, were divided and conquered through the BIT-

⁶¹ See Douglas, Z., *The International Law of Investment Claims* chapter 2 rule 13 section F.

⁶² See Schreuer, C., *The ICSID Convention: A Commentary, Second Edition* the Authors' Preface to the Second Edition.

⁶³ See Dolzer, R. and Schreuer, C., *Principles of International Investment Law* page 18.

⁶⁴ See Sornarajah, M., *The International Law on Foreign Investment, 3rd edition* chapter 5 page 172.

⁶⁵ See Leeks, A., *The Relationship Between Bilateral Investment Treaty Arbitration and the Wider Corpus of International Law: The ICSID Approach* section II.

⁶⁶ As an example of such a provision, see article 4 of the US Model BIT of 2004.

variant of the prisoners dilemma.⁶⁷ Whatever the reason, the outcome is that the BIT system currently in force conveys a lot of substantive rights to foreign investors that are anchored at the level of public international law. So far this has been mostly beneficial to the developed countries of the western hemisphere since they historically have been the major global capital exporters. As some developing countries are reaching maturity, however, the bilateral character of their treaties may slowly start to kick in,⁶⁸ possibly heralding a calibration of the view on BITs among the international community at large.⁶⁹

2.2.5 *Municipal law*

Being often substantial, complex and costly, foreign investments frequently interrelate with the host state society on multiple planes. The juridical aspects of the investor-state relationship are thus, to some extent or other, intertwined with municipal law.⁷⁰ In what way and magnitude this is the case depends upon the interconnection between the sources of law of the specific investment relationship at hand.⁷¹ Since municipal law often is more consistent, exhaustive and inherently capable of regulating all of the aspects of the investor-state relation than sources of international law, a minimum position would be to assert that municipal law governs any aspects not primarily governed by any other sources of law.⁷² Nevertheless, the choice of law question in relation to what extent municipal law

⁶⁷ See Guzman, A., *Why LDCs Sign Treaties that Hurt Them: Explaining the Popularity of Bilateral Investment Treaties* page 666.

⁶⁸ See Van Aaken, A., *Perils of Success? The Case of International Investment Protection* section 5, in particular page 25.

⁶⁹ For a discussion on this within a NAFTA context, see Alvarez, G. A. and Park, W. W., *The New Face of Investment Arbitration: NAFTA chapter 11* part VI.

⁷⁰ For instance municipal commercial law, company law, administrative law, labour law, tax law, foreign exchange regulation, real estate law and environmental law among other legal subjects.

⁷¹ See section 2.3 below.

⁷² The ICSID Convention takes a small step further in stating, in its article 42, that a tribunal shall apply host state law and applicable rules of international law in the absence of an agreement on governing law between the investor and the host state. It would generally seem that ICSID jurisprudence favours the theory of a supplemental and corrective function of international law vis-à-vis domestic law. See for instance *Amco v*

is to govern the foreign investment under scrutiny is frequently an area of high dispute that still draws a lot of ink in both theory and practice.

An indisputable position, however, is that municipal law, to a certain extent, necessarily must be present at the outset of any foreign investment affair as the law applicable to issues concerning the existence and scope of the property rights the investor is to be granted.⁷³ Furthermore, since there is no coherent international law of contract,⁷⁴ it may be that some aspects of any contractually based investor-state relationship also must be founded on municipal law.⁷⁵ More specifically, the question of whether the host state is party to any investment contract must inevitably depend on some legal system prior to the contract, and the municipal law of the host state itself is hereunder an obvious choice.⁷⁶ Some commentators have argued that it is unsatisfactory to open for the possibility that the state party be entitled to rely on its own law to escape from a contract it freely entered into, though: Any question of the existence of a contractual commitment should rather be qualified as an issue of arbitrability.⁷⁷ This fairly theoretical discussion of a subject with deep doctrinal undertones will not be further developed here in a section that merely is aimed at highlighting the possible basic applicability of municipal law.⁷⁸ It also falls outside the scope of this thesis as such.

Indonesia: Decision on Annulment paragraph 20, as well as Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter X section 2 pages 269-270.

⁷³ See Douglas, Z., *The International Law of Investment Claims* chapter 2 rule 4.

⁷⁴ See section 2.2.2 above.

⁷⁵ See hereunder the quotation from the *Serbian Loans Case* of note 51 above.

⁷⁶ See Blackaby, N. and Partasides, C., with Redfern, A., and Hunter, M., *Redfern and Hunter on International Arbitration, 5th Edition* chapter 2 section C subsection (a) part (iii).

⁷⁷ See for instance Gaillard, E. (ed.) and Savage, J. (ed.), *Fouchard, Gaillard, Goldman on International Commercial Arbitration* part 2 chapter II paragraph 539.

⁷⁸ The discussion would lead back to a question of whether, and to what extent, a state fundamentally may bind itself with respect to its territorial sovereignty and national autonomy. For an in depth review of the topic, see Alvik, I., *Contracting with Sovereignty: State Contracts and International Arbitration*.

2.3 Methodology

As previously stated, international investment law is the name of the body of law governing foreign investments in their aggregate. On the individual level however, quite dissimilar mixtures of sources of legal authority may govern the specific investment relationship at hand. The varying mix-ups of municipal law, BIT law, MIT law, customary international investment law and investment contract law constitute legal issues of *sui generis* character. Thus, the particular content of international investment law varies considerably relative to the case under scrutiny. Never the less, some common denominators and arrangements may be identified. The following paragraphs aim at outlining a framework along a few such structural axes, applicable over all international investment affairs.

The various sources of law explored in section 2.2 have, in the lack of a better word, a somewhat liquid relationship under international investment law. One possible reason behind this fluidity is that international investment law, as opposed to municipal law and to a certain extent also public international law and international commercial law, possesses no formal backbone of a constitutional character.⁷⁹ How then should a dispute regarding a foreign investment be approached?

An investment dispute may in principle be solved through municipal law in national courts. In that case the methodology is given by the national legal system of the state in question. This conflict-resolution alternative has limited usefulness when it comes to juridical disputes between a state and a foreign investor, though: Since the state party to the investor-state relationship enjoys monopoly on legislative power through its territorial sovereignty,⁸⁰ it may change the rules of the game, with fatal consequences for the investor, as long as it keeps itself within the confines of its own constitutional framework and its duties under international law. The investor, fearing the event of a state intervention and naturally trying to limit his risks along all axes, must thus either rely on the capacity of municipal law for getting the potential intervention overruled, or hope that the shackles of

⁷⁹ See Wittich, S., *The Limits of Party Autonomy in Investment Arbitration* section 2.2.

⁸⁰ See Brownlie, I., *Principles of Public International Law 7th Edition* part III chapter 6.

international law may limit the host state's legislative latitude. But because the state party in most cases holds the relative expertise on municipal law, since it has the power to adjust it and since national courts often will have a tendency to favour the state in a dispute with an alien, the investor does generally not prefer the former alternative.⁸¹ Instead he will try to rely on the protection of international law. As a consequence, international investment law, as seen in section 2.2, crystallized out of a need for a system to tackle such conflicts.

Lacking alternatives, disputes regarding international investments are thus usually resolved through arbitration, either of the ad hoc kind or within the boundaries of a more permanent authority such as the ICSID. In both cases, customary law of international investment, whatever its content, must be taken into account due to its overreaching character within the context of international investment law per se.⁸² Whether, and to what extent, a certain BIT, MIT, municipal law or investment contract should be given relevancy however, depends upon the specific investment relationship at hand.⁸³ If, for instance, the arbitration proceeding in question was initiated under the provisions of a BIT, it follows logically that it is the same BIT that primarily must be relied upon as the source of law governing that arbitration, both on the substantive and procedural level, as far as itself provides for.⁸⁴ Choice of law or similar provisions within that BIT may though subsequently, directly or indirectly, draw one or more of the other sources of law explored above into the fray.⁸⁵ In the case of a lacuna, *renvoi*⁸⁶ may be made to the municipal law of the host state or the place of arbitration, or similar sets of rules, at the discretion of the arbitration tribunal.⁸⁷

⁸¹ See Sornarajah, M., *The International Law on Foreign Investment*, 3rd edition chapter 7 section 2 page 289 and section 1.1.3 page 286.

⁸² See Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter I section 5 page 24.

⁸³ See *Compañía de Aguas del Aconquija v Argentina: Decision on Annulment* paragraphs 95-96.

⁸⁴ See Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter X section 2 subsection (f) introduction and (j) page 266.

⁸⁵ See *ibid.* chapter X section 2 subsection (j).

⁸⁶ The term *renvoi* refers in this context to some municipal law being made applicable due to a lack of regulation in the relevant international investment law.

⁸⁷ See Newcombe A. and Paradell L., *Law and Practice of Investment Treaties* chapter 2 §2.13.

The relevant sources of law must subsequently, necessarily, be interpreted before they can be applied. As international treaties, BITs and MITs are subject to interpretation under article 31 of the Vienna Convention on the Law of Treaties.⁸⁸ Thus they shall in principle be ‘interpreted in good faith in accordance with the ordinary meaning given to the terms of the treaty in their context and in the light of its object and purpose’.⁸⁹ The fact that *de facto* lapses have occurred from this method,⁹⁰ does not limit its fundamental applicability. As for preparatory work and interpretive statements, such supplementary means of interpretation have a tendency to be taken into account if available (which they seldom are, with the exception of interpretive statements from the NAFTA Free Trade Commission)⁹¹ in accordance with the Vienna Convention article 32.⁹² Since each tribunal is constituted for the particular case at hand however, there may be no similar direct reliance on precedence in the interpretation process.⁹³ Articulations of prior tribunals may nevertheless be heeded relative to their persuasiveness. In this context, see also the Vienna Convention article 31 paragraph 3 alternative (b) which states that ‘any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its

⁸⁸ A multitude of arbitration awards confirm this point, see for instance *AAPL v Sri Lanka* paragraphs 38-42, *Siemens v Argentina: Decision on Jurisdiction* paragraph 80 and *Methanex v United States* paragraphs 15-23. Also see Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter II section 1.

⁸⁹ In other words, a tribunal interpreting an investment treaty is to find the intention of the treaty parties. Note at this point though, the peculiar aspect of international investment law arbitrations in that only one of the parties to the arbitration (the state party) is a direct party to the treaty. As Sir Franklin Berman points out in his dissenting opinion to the *Empresas Lucchetti v Peru: Decision on Annulment and Dissenting Opinion* award (paragraph 9 in particular), the tribunal should thereby treat the interpretive process relating to the intentions of that treaty party with all due caution.

⁹⁰ For instance *SGS v Pakistan: Decision on Jurisdiction* paragraph 171.

⁹¹ See McLachlan, C., *Investment Treaties and General International Law* part I section C page 372.

⁹² See Newcombe, A. and Paradell L., *Law and Practice of Investment Treaties* chapter 2 §2.28. Though acknowledging that such sources are scarce, Roberts, A., *Power and Persuasion in Investment Treaty Interpretation: The Dual Role of States* argues for a stronger reliance on subsequent agreements and practice (in accordance with article 31 paragraph 3 alternatives (a) and (b) of the Vienna Convention) when interpreting investment treaties.

⁹³ See for instance *AES Corp. v Argentina: Decision on Jurisdiction* paragraphs 17-33.

interpretation' should be taken into account.

A few notes about precedence within the ICSID system are at this point perhaps merited. The formal starting point here mirrors the one outlined above in that all tribunals are established on *ad-hoc* basis, and are thus not in principle compelled to follow the reasoning of prior tribunals.⁹⁴ Recent jurisprudence, however, would appear to somewhat calibrate this position by stressing that tribunals have a duty to contribute to a harmonious development of international law through adopting, unless subject to compelling contrary grounds, any solutions established by consistent case law.⁹⁵ Some commentators argue that this constitutes a *de facto* doctrine of precedence.⁹⁶ This thesis will not further discuss the matter beyond pointing out that even if it would go too far to claim that the ICSID system relies on a *de facto* doctrine of precedence, its constituent tribunals at least exhibits a tendency to be persuaded by the reasoning of prior tribunals.⁹⁷ Due to the ICSID's inclination towards taking their appointments very seriously,⁹⁸ that argument is even more potent if the prior tribunal in question was an ICSID Annulment Committee.

Moving on from the interpretation of BITs and MITs to the interpretation of investment contracts, such practice is in essence, in the event of a dispute, a prerogative of the arbitration tribunal at hand, unless something else is provided for, directly or indirectly, by the contract itself (within a provision that in turn also must be interpreted). This follows as a logical consequence of party autonomy as the premise for this kind of arbitration.⁹⁹ It may here be noted that in terms of establishing the tribunal's jurisdiction on the basis of a contract, which essentially must be the starting point of any such arbitration, the tribunal is

⁹⁴ Article 53 of the ICSID Convention holds that an award is binding on the parties to the dispute, resembling article 59 of the Statute of the ICJ which enunciates that 'the decision of the Court has no binding force except between the parties and in respect of that particular case'.

⁹⁵ See *Saipem v Bangladesh: Decision on Jurisdiction* paragraph 67.

⁹⁶ See Di Pietro, D., *The Use of Precedents in ICSID Arbitration: Regularity or Certainty?* page 96.

⁹⁷ See Schreuer, C., *Diversity and Harmonization of Treaty Interpretation in Investment Arbitration* part III page 17 and onward.

⁹⁸ See Sweet, A. S., *Investor-State Arbitration: Proportionality's New Frontier* part IV page 72.

⁹⁹ See section 2.2.2 above.

entitled to do so itself through the customary principle known as *kompetenz-kompetenz*.¹⁰⁰ The operative methodology is thereby for the tribunal to decide upon based on the arbitration clause that constitutes it. In the event of confusion, the interpretation of that arbitration clause may be subject to municipal law at the place of arbitration in accordance with the Convention on the Recognition and Enforcement of Foreign Arbitral Awards article V (the New York Arbitration Convention).

Having now briefly sketched out the interpretive principles of international investment law, the only issue left is to embellish on the interrelationship between the different sources of law encountered. As already mentioned; by accepting arbitration through a specific instrument (for instance a BIT or an investment contract) the parties to the dispute also accept the other provisions within that source of law. If it (as often is the case) contains a choice of law provision listing several other sources of law as relevant, then all of these must also be taken into account by the tribunal.¹⁰¹ The subsequent ranking and application of those sources is but a process of interpretation as has been explored just above. Furthermore, the different sources of international investment law are at the outset complimentary rather than alternative in the sense that the application of one does not automatically exclude application of the others. This follows from the distinction between contract claims and treaty claims laid down in the *Vivendi I* case and its subsequent annulment decision.¹⁰² It would seem that both subsequent arbitration practise¹⁰³ and juridical commentators¹⁰⁴ also have endorsed the sentiment.

¹⁰⁰ See Blackaby, N. and Partasides, C., with Redfern, A., and Hunter, M., *Redfern and Hunter on International Arbitration*, 5th Edition chapter 5 section D subsection (c) part (iv). As for ICSID tribunals, the *kompetenz-kompetenz* principle is laid down in the ICSID Convention article 44.

¹⁰¹ In the *CME v Czech Republic: Final Award*, the tribunal argued in paragraph 402 that it did not have to take into account all of the listed sources of law. The award has been thoroughly criticized both in Begic, T., *Applicable Law in International Investment Disputes* chapter II section 2 page 39 and elsewhere, however.

¹⁰² See the *Compañía de Aguas del Aconquija v Argentina* award paragraphs 53-54 and the *Compañía de Aguas del Aconquija v Argentina: Decision on Annulment* paragraphs 95-103.

¹⁰³ For instance *Impregilo v Pakistan: Decision on Jurisdiction* paragraphs 274 and 291.

¹⁰⁴ See Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter X section 2 subsection (a) part (dd) and Subedi, S. P., *International Investment Law: Reconciling Policy and Principle*

In the event of an impossibility to separate a contractual claim from a treaty claim, some awards have held that treaty tribunals would anyhow have jurisdiction on the matter at hand, implying ascendancy relative to tribunals constituted on a contractual basis.¹⁰⁵ Other awards have been reluctant to accept that position whole-heartedly however.¹⁰⁶ Also, a so-called umbrella clause in a treaty may fundamentally affect the question,¹⁰⁷ though such an incidence would exclusively depend on the process of interpretation of the treaty at hand, and in essence be outside the sphere of the contract as such. All in all, a final clarification on the interrelation between international investment contract and treaty law, and through it contract claims and treaty claims, is still pending.

Though there are both additional methodological issues and a corpulent body of literature tackling both these and the matters now presented out there, it would go beyond the scope of thesis to further expand on such topics at this point. Suffice it to conclude that the methodology of international investment law ultimately may be characterized as somewhat inconclusive in its present state.

2.4 What constitutes an investment?

The question of what constitutes an investment, and therefore is protected under international investment law, may to some extent, in accordance with the methodology presented above, be directly regulated by the source of law governing the investment relationship at hand, be it a BIT, a MIT or an investment contract. Article 1 of the 2004 US Model BIT for example holds that ‘every asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, including such characteristics as the commitment of capital or other resources, the expectation of gain or profit, or the

chapter 5 pages 146-148.

¹⁰⁵ See *Aguas del Tunari v Bolivia: Decision on Jurisdiction* paragraph 119 and Tawil, G. S., *The Distinction Between Contract Claims and Treaty Claims: An Overview* section II page 500.

¹⁰⁶ See *Waste Management v Mexico* paragraph 174 for instance.

¹⁰⁷ An umbrella clause typically states that any investment contract entered into between a state and a national of another state shall be honoured, thus elevating a breach of contract to a breach of treaty. See for instance the German Model BIT of 2008 article 7 paragraph 2.

assumption of risk' is regarded as an investment. In practise however, things have often gotten complicated as the definition to be relied upon turned out not to be precise enough, or even non-existing.

As an example of the latter, article 25 of the ICSID Convention states that 'the jurisdiction of the [ICSID] shall extend to any legal dispute arising directly out of an investment'. No further definition of "investment" is included. A dispute as to how far that investment concept thereby stretches was bound to follow. The disagreement revolves mainly around whether or not so-called "portfolio investments" should be covered. These are set apart from more the more direct variant of foreign investments by the investor being, though owning it, without direct control of the asset.¹⁰⁸ Thereby it would in principle be possible for a national investor to increase the magnitude of legal protection for his investment by setting up a holding company for the investment in another state, and the same goes for any third country investor with less protection than what he would have been entitled to through a different state than his own. Case law regarding article 25 seems to have established four criteria for the determination of what constitutes an investment (contribution of the investor, duration of the project, existence of operational risk and contribution to the host state development).¹⁰⁹ These will not be further dealt with here.¹¹⁰ It should, though, perhaps be noted that the term "investment" under ICSID article 25 usually is interpreted autonomously of other sources of international investment law.¹¹¹ Furthermore, different ICSID tribunals' approaches to the question have been, and continues to be, somewhat diversified.¹¹²

In general, there currently seems to be a certain dispute among juridical commentators

¹⁰⁸ See Dolzer, R., *The Notion of Investment in Recent Practice* page 263.

¹⁰⁹ See *Fedax v Venezuela: Decision on Jurisdiction* paragraphs 21-43 and *Salini v Morocco: Decision on Jurisdiction* paragraph 52 as well as Dolzer, R. and Schreuer, C., *Principles of International Investment* chapter III section 2 subsection (c).

¹¹⁰ Instead see Schreuer, C., *The ICSID Convention: A Commentary, Second Edition* chapter II article 25 section II part D.

¹¹¹ See instead Dolzer, R. and Schreuer, C., *Principles of International Investment* page 61.

¹¹² See Gaillard, E., *Identify or Define? Reflections on the Evolution of the Concept of Investment in ICSID Practice* section A.

whether, in the absence of a clearer definition, only direct investments may be defined as “investments”, or if portfolio investments also are covered by the term.¹¹³ The criteria usually presented to exclude the latter position are that the investment venture must involve a transfer of funds regarding a longer-term project of some business-risk with the purpose of regular income and with the participation of the investor, at least to some extent, in the management of the project.¹¹⁴ Precluding portfolio investments from protection, this definition would, in turn, limit the previously mentioned nationality shopping problem as well as the problem of multiple cases of arbitration filed from the same dispute.¹¹⁵ However, many BITs¹¹⁶ as well as chapter 11 of the NAFTA¹¹⁷ indeed contain a clearer definition of “investment” that definitely includes investments of the portfolio kind. Following the historical trend,¹¹⁸ it has so far been the net capital exporting states that champion a wider definition of the investment concept (in BITs, MITs and in general), while the net capital importing states typically have been somewhat more reserved.¹¹⁹

Along a second line of inquiry lies the question of which facets of the investments should be given protection. Again, this may be regulated directly by the relevant sources of law. In the absence of a precise enough definition however, some manner of general concept must be relied upon in the interpretation process: There is no doubt that the

¹¹³ Against this view see Sornarajah, M., *The International Law on Foreign Investment*, 3rd edition chapter 1 section 1.1. A risk-based argument for it may be found in Brownlie, I., *Treatment of Aliens: Assumption of Risk and International Law* page 311 as well as in Douglas, Z., *The International Law of Investment Claims* chapter 5 rule 23.

¹¹⁴ See Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter III section 2 subsection (a).

¹¹⁵ Under a definition of investment that includes portfolio investments, both the investor (directly) and the owner of the investor (as the holder of a portfolio investment) would be able to file a case in the event of a single dispute with the host state. As an example, see the Lauder cases: *CME v Czech Republic: Final Award* together with *Lauder v Czech Republic*.

¹¹⁶ See for instance the US Model BIT of 2004 article 1 or the Canadian Model FIPA of 2003 article 1.

¹¹⁷ See NAFTA article 1139.

¹¹⁸ See section 2.2.

¹¹⁹ See the ASEAN Framework Agreement on Investment article 2 which explicitly excludes portfolio investments from its definition of “investment”.

tangible side of the asset is protected. This follows logically from the investment concept already developed. Furthermore, there seems to be a general consensus that protection also stretches over the intangible side of the asset, as well as to any administrative rights that are necessary for the operation of the investment project.¹²⁰ In the case of a lack of boundaries for the concept of intangibility or the substance of the administrative rights, *renvoi* may be made to municipal law of the host state.¹²¹ Additionally, arguments stating that pre-investment expenditures too should be covered by investment protection have been advocated. It would seem, though, that ICSID tribunals not have supported this view in *Mihaly v Sri Lanka* paragraph 61 and *PSEG v Turkey: Decision on Jurisdiction* paragraphs 67-105. Juridical commentators however, currently appear to be somewhat undecided on the issue.¹²² All things considered, the historical trend has been to add more and more facets of the investment concept to the sphere of protection; a practice facilitated mainly by the net capital exporting states through the medium of BITs. As was the case concerning the evolution of substantive rights conveyed to foreign investors though, this trend might start to turn as the bilateral character of the BITs between (the historically) net capital importing and exporting states becomes more pronounced.¹²³

¹²⁰ See Sornarajah, M., *The International Law on Foreign Investment*, 3rd edition chapter 1 page 16 and Schreuer, C., *The ICSID Convention: A Commentary*, Second Edition chapter II article 25 section II part D paragraph 140.

¹²¹ See Douglas, Z., *The International Law of Investment Claims* chapter 5 rule 22 paragraph 352.

¹²² For the notion see Douglas, Z., *The International Law of Investment Claims* chapter 5 rule 22 section D subsection (viii), against it see Sornarajah, M., *The International Law on Foreign Investment*, 3rd edition chapter 1 pages 16-17.

¹²³ See Van Aaken, A., *Perils of Success? The Case of International Investment Protection* section 5.

3 Proportionality

This chapter will introduce the basic concept of proportionality as such, as well as place it within its present juridical frame of reference. The intention here is to provide a general definition of proportionality, as well as a review of what the conception embodies in its pure form. Chapter 5 will subsequently take the established concept, and assess its utility within the sphere of international investment law specifically.

Starting off with a basic explanation of proportionality in section 3.1, chapter 3 will move on to look at concept's current diffusion throughout municipal and international law in section 3.2. Sections 3.3 and 3.4 will subsequently, to a certain extent, foreshadow chapter 5 by on the one hand roughly sketching out proportionality's current applicability within the specific context of international investment law, and on the other by indicating how environmental considerations generally may relate to proportionality.

3.1 The concept

A tribunal may from time to time find itself in a position where it has to equate two or more differing legal positions; be they norms, interests or values. In such a situation, assuming that it may not pronounce itself unequal to the task, the tribunal is forced to in some way match the positions against one another and award a partial or complete victory to one over of the others to the extent of their incompatibility. One obvious question thus manifesting itself is how such a procedure should be undertaken.

The answer to this question may partially be a function of the character of the positions to be equated. Adopting the dichotomy of Ronald Dworkin, some juridical positions, characterized as rules, apply in an all-or-nothing demeanour, while others, characterized as principles, are more relatively disposed.¹²⁴ If faced with a conflict between the former, the

¹²⁴ See Dworkin, R., *Taking Rights Seriously* chapter 2 pages 24-26.

very nature of these rules in claiming absolute validity necessarily results in the tribunal having to choose absolutely between them, by definition prevented from reaching any kind of middle ground decision. This thesis does not further concern itself with such situations. Faced with a conflict of principles on the other hand, the tribunal may choose from a much wider range of possible structural outcomes since the latter, as opposed to rules, are realizable to different degrees, and may thus be balanced against one another.¹²⁵ Balancing, in turn, is fundamentally an appealing juridical prospect in that it provides an opportunity for flexibility and elasticity, bestowing the tribunal with the authority to take into account the entire contextual field in its award and thereby fashion the most equitable judgement possible. The flip side though is that the same flexibility and elasticity may raise anxieties about whether it awards too much authority to the tribunal at the cost of juridical predictability and contractual freedom: Can the tribunal ever truly be constrained *ex ante*, and may it always reach any decision it wants?¹²⁶ Such fears, however, may be mitigated if some degree of certainty and stability as to how the tribunal approaches the balancing is established. The basic legitimacy questions of consistency and adequate juridical credence may thus be adequately accommodated at the procedural level.¹²⁷ The initial question outlined above thereby still remains, though: How should the tribunal actually undertake the balancing procedure?

A number of standards of review have been proposed, and a range of alternatives is practiced. One specific possibility is known as proportionality. It proposes that the tribunal, faced with a conflict between legal principles, conducts an analysis based on a specific procedural framework made up of three cumulative steps, thereby ensuring that sufficient respect is paid to the positions of both of the parties to the dispute. First, it must assure itself that any specific measure advocated is suitable by requiring ‘a causal relationship

¹²⁵ See Kingsbury, B. and Schill, S., *Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law* part III pages 21-22.

¹²⁶ The issue, in short, is the second order legitimacy problem of judicial lawmaking. See Sweet, A. S., *Investor-State Arbitration: Proportionality's New Frontier* part III section B.

¹²⁷ See Sweet, A. S. and Mathews, J., *Proportionality Balancing and Global Constitutionalism* part II (in particular section D).

between the measure and its objective'¹²⁸. Second, it must assess the measure's necessity by requiring that 'the objective, upon which the measure is based, cannot be achieved by alternative means that are less restrictive than the measure adopted'¹²⁹. Finally, it must conduct a proportionality analysis in the strict sense of the word, *stricto sensu*, analyzing 'whether the effects of [the] measure are disproportionate or excessive in relation to the [other] interests affected'¹³⁰. Each of these three steps will be further addressed in turn below. It should furthermore already at this point be discernable that proportionality is but a method of (or framework for) conducting juridical balancing operations. The concept therefore in principle does not, as shall be further discussed in section 3.1.4, concern itself with a question of how intensely the tribunal actually should review a measure relative to its purported aim. This issue is usually termed "intensity of review" or "margin of appreciation".

3.1.1 Suitability

The first step of the proportionality analysis is commonly known as "suitability". That any measure, to possess cogency in relation to the principle it claims applicable, needs to be suitable or appropriate to achieve the objective it pursues, is more or less self evident: Under any other scenario, the argumentation of the party advancing that measure would rest on a logical fallacy in that no causal relationship between the measure and its scope would exist. This step is thus intended to insure that the measure advocated is rational in relation to its purported end.¹³¹ Any quantitative or qualitative review beyond mere causality, however, is not contemplated at this stage of the analysis.¹³²

¹²⁸ Jans, J. H., *Proportionality Revisited* page 240.

¹²⁹ Andenæs, M. and Zleptnig, S., *Proportionality: WTO Law in Comparative Perspective* chapter II section E part 2 page 389.

¹³⁰ Ibid. chapter II section E part 3 page 390.

¹³¹ See Trachtman, J. P., *Trade and ... Problems, Cost-Benefit Analysis and Subsidiarity* section I part C page 35. Note that this assessment is objective as to the causality reviewed. It should therefore not be confused with an intensity of review issue. See section 3.1.4 below.

¹³² Within the context of the WTO, this is stated in *Brazil – Measures Affecting Imports of Retreaded Tyres*

Note that, as Andenæs and Zleptnig point out, a tribunal will, in the context of suitability, also have to determine whether to look at the measure from an *ex post* or an *ex ante* perspective.¹³³ Such a difference in scope might affect the procedure under this first stage of the proportionality review, and it might also influence the review under the necessity and proportionality *stricto sensu* stages: In *Continental Casualty Company v Argentina* paragraph 198 (as shall be further discussed below) the tribunal seems to consider the measure in question from both perspectives at the necessity stage, prompting the question of whether the analysis there undertaken can properly be considered an actual proportionality analysis at all.

3.1.2 Necessity

Having found that the measure in question was suitable, the tribunal next has to evaluate whether it was necessary. The necessity test aims at assessing whether the measure was the least restrictive reasonably available alternative capable of achieving the objective sought. It thus rests on the argument that if faced with a choice of equally appropriate measures, the least onerous one should be selected.¹³⁴ Functionally, this equates into, first, a question of whether less restrictive reasonably available measures exist, and second, a question of whether the measures then considered are equally effective in pursuing the objective sought.¹³⁵ In some cases, tribunals of various varieties have jumbled both of these questions together with the proportionality *stricto sensu* test into a combined, often somewhat opaque, necessity-proportionality *stricto sensu* analysis.¹³⁶

paragraph 147.

¹³³ See Andenæs, M. and Zleptnig, S., *Proportionality: WTO Law in Comparative Perspective* chapter II section E part 1.

¹³⁴ See Snell, J., *Goods and Services in EC Law: A Study of the Relationship Between the Freedoms* chapter 4 part 4 section B page 198.

¹³⁵ See Ortino, F., *Basic Legal Instruments for the Liberalisation of Trade: A Comparative Analysis of EC and WTO Law* chapter 4 section 4.3 page 471.

¹³⁶ In the context of international investment law for example, see *Tecmed v Mexico* paragraphs 122 onward, while in the context of WTO law see *Korea – Various Measures on Beef* paragraphs 164 onward.

Some commentators also seem to endorse such a practice as the proper understanding of proportionality.¹³⁷ Under a more sophisticated understanding of the standard, however, the first of the mentioned questions sets the scope of the necessity stage by putting the emphasis on the comparison between the measure advocated and other, alternative, measures, thereby functionally insulating this test from the proportionality *stricto sensu* test. Consequently, any jumbling of the necessity and the proportionality *stricto sensu* stages into one combined analysis will be structurally flawed, and probably best avoided by tribunals striving for clarity and consistency. Tribunals following the formal proportionality framework would dodge this problem.

Another crucial component of the necessity test is its inherent reasonability. If absent, the necessity stage would almost without exception invalidate the measure in question since conceivable alternatives more or less always would exist if their costs were to be disregarded. In other words, a measure may be necessary even though it is not indispensable.¹³⁸ WTO practice on the necessity stage of the standard of review utilized seems to confirm this in stating that ‘the requirement [...] that a measure be "necessary" – that is, that there be no "reasonably available", [...] alternative – reflects the shared understanding [...] that substantive [...] obligations should not be deviated from lightly. An alternative measure may be found not to be "reasonably available", however, where it is merely theoretical in nature’¹³⁹. Since surprisingly little theory and practice touch on the reasonability component of the necessity test elsewhere, this quote would seem to sum up the present state of affairs nicely.

A subsequent question concerns what the reasonability requirement actually contains. Its wording points to an analysis of the costs of the suggested alternative measure relative to those of the measure under scrutiny. If the gap is unreasonably large, the alternative falls. Note at this point that the reasonability only relates to the party advancing the

¹³⁷ See for instance De Schutter, O., *International Human Rights Law* part II chapter 3 section 3 subsection 3.4 pages 313-314.

¹³⁸ See Regan, D. H., *The Meaning of ‘Necessary’ in GATT Article XX and GATS Article XIV: the Myth of Cost-Benefit Balancing* section 3 page 354.

¹³⁹ *US – Gambling* paragraph 308. See also *Korea – Various Measures on Beef* paragraph 165.

measure in question. The analysis conducted is therefore functionally separate from the proportionality *stricto sensu* analysis that relates the measure to any norms, interests and values of the opposing party. As for the mentioned gap itself, its threshold value will, it seems, lacking any formally binding criteria or assertions, need to be determined on a case-for-case basis.

Finally, a necessity analysis is almost inevitably a *post-hoc* assessment by the tribunal conducting a balancing procedure. That tribunal thus has, unlike the parties to the dispute at the time of an approaching crisis, the benefit of hindsight. If the measure under scrutiny turns out successful in limiting or preventing said crisis, the crisis' potential may often appear less grave in retrospect, thereby reducing the chances of the measure passing the necessity and proportionality *stricto sensu* tests.¹⁴⁰ While the latter evidently is directly affected since it compares the effects of the measure with its adverse consequences, the influence on the necessity test is more indirect in altering the course of events relative to the perceived development towards the crisis. Thus, the appropriateness, restrictiveness and reasonableness of the flora of available measures might appear different in retrospect than it did to the parties at the time of implementation of the measure. Any tribunal utilizing the proportionality framework should bear this possibility in mind to minimize the chances of adverse awards.

3.1.3 Proportionality *stricto sensu*

If a certain measure passes both the suitability and the necessity stages, a tribunal utilizing the proportionality framework for balancing will then conduct the formal proportionality analysis; proportionality *stricto sensu*. Note at this point that the proportionality framework offers a nested sequence of steps: Any measure in question may only be reviewed under the next stage if it survived the review under the previous one. The proportionality *stricto sensu* stage will therefore often not be reached since the measure under review frequently has been disposed of during the preceding stages.

Under its proportionality *stricto sensu* analysis the tribunal examines whether the

¹⁴⁰ See Bjorklund, A. K., *Emergency Exceptions: State of Necessity and Force Majeure* part 5 section B.

effects of the suitable and necessary measure are incommensurate relative to any adverse consequences it would exercise on other interests affected by the implementation of the measure.¹⁴¹ Even though the measure was necessary when viewed in relation to possible alternative measures, it might still be considered too much when assessed in the context of the other norms, interests and values it would frustrate. In an illustrative example of such an assessment, the European Court of Justice (ECJ) held, in the *Stoke-on-Trent v B&Q* case, that ‘appraising the proportionality of national rules which pursue a legitimate aim under Community Law involves weighting the national interest in attaining that aim against the Community interest in ensuring the free movement of goods’¹⁴². In that case, the measure in question, the national rules, did not overly hamper the opposing position, the Community interests in the free movement of goods, and was thus deemed proportional.

At this point, the structural difference between the necessity stage and the proportionality *stricto sensu* stage is becoming more discernable. The latter is an indispensable part of the proportionality framework in the sense that ‘any measure at all could be presented as “necessary” if the purpose they serve is defined in wide enough terms’¹⁴³. Thus, the proportionality *stricto sensu* stage is needed in order for the tribunal to be able to, in its balancing process, not only assess the measure under scrutiny against alternative measures promoting the same end, but also against other norms, interests and values supporting differing perspectives.

In fact, proportionality even gets its name from the proportionality *stricto sensu* stage. The latter being the *modus operandi* that separates proportionality from the other standard of review alternatives,¹⁴⁴ it more or less defines the proportionality standard as such, even though it, as seen, is but the final test of the three-step framework. This equates into some terminological issues: Both commentators and practitioners do from time to time muddle

¹⁴¹ See Andenæs, M. and Zleptnig, S., *Proportionality: WTO Law in Comparative Perspective* chapter II section E part 3.

¹⁴² *Stoke-on-Trent v B&Q* page I-6658.

¹⁴³ Lerche, P., *Übermaß und Verfassungsrecht: Zur Bindung des Gesetzgebers an die Grundsätze der Verhältnismäßigkeit und der Erforderlichkeit* chapter 1 page 20.

¹⁴⁴ See sections 3.3.1 and 5.1.4.

their argumentation (and thereby the debate relating to standards of review in international investment law) by using the term “proportionality” without clearly defining whether they are referring to the standard of review alternative or the proportionality *stricto sensu* test specifically.¹⁴⁵ This thesis always refers to the former when it invokes the proportionality expression.

Moving back into the proportionality framework, another question faced is at what level the tribunal should place its proportionality *stricto sensu* review. Should it balance the competing norms, interest and values against each other on a principle level exclusively, should it take into account the entirety of factual circumstances of the case at hand or should it place the review at some point in between? Case law over several juridical subjects has shown a tendency to situate the balancing at a fairly concrete level: The ICSID articulates a somewhat tangible standard in *Tecmed v Mexico*,¹⁴⁶ the ECJ in general seems to take into account the specific disadvantages for the person whose rights have been frustrated,¹⁴⁷ and WTO tribunals also have been rather specific when conducting their proportionality analyses.¹⁴⁸ Note, however, that all of the cited practice additionally takes into account theoretical argumentation in its assessments.

The balancing conducted during the proportionality *stricto sensu* stage should furthermore be discerned from strict economic interest balancing. While the latter involves a quantitative review of opposing interests equated into a common currency (often monetary value), the former encompasses a broader approach of both quantitative and qualitative character.¹⁴⁹ While both options necessarily aim at achieving the most pareto-optimized result possible given the situation,¹⁵⁰ their scopes differ: Economic interest balancing is, though possibly quite complex, fundamentally only the name of a certain

¹⁴⁵ See for instance *Tecmed v Mexico* paragraph 122 and Franck, T. M., *On Proportionality of Countermeasures in International Law*.

¹⁴⁶ See *Tecmed v Mexico* paragraph 122.

¹⁴⁷ See for instance the *Pfizer* case paragraphs 411-413.

¹⁴⁸ See for instance *Korea – Various Measures on Beef* paragraphs 152 onward and *Brazil – Measures Affecting Imports of Retreaded Tyres* paragraphs 133 onward.

¹⁴⁹ See Engle, E., *The History of the General Principle of Proportionality: An Overview* part II section C.

¹⁵⁰ See Alexy, R., *A Theory of Constitutional Rights* chapter 3 part III section 2 page 102.

mathematical summation. Proportionality *stricto sensu* on the other hand, refers to a more subtle operation under which both qualitative and quantitative arguments are discerned and weighted against one and other. On a more philosophic level, the methods may, deterministically speaking, not be fundamentally separate entities. However, in the context of this thesis, the difference materializes in that while economic interest balancing refers to a process with the articulated aim of evaluating all factors of an issue in terms of an *ex ante* reviewable common currency summation, proportionality *stricto sensu* makes no claim beyond referring to an operation of balancing from which a result is procured.¹⁵¹

3.1.4 *Intensity of review*

Alongside the question of which standard of review it should apply to a balancing procedure lies the question of what intensity of review the procedural authority should exercise.¹⁵² Though the latter not is the central topic of this thesis, it nevertheless merits some notes in order to clarify the proportionality principle in terms of what it does not concern. While proportionality constitutes a procedural framework a tribunal may use for balancing two or more competing norms, interests and values, intensity of review refers to the rigour of scrutiny the tribunal employs during the balancing process relative to the legality of the measures reviewed. In other words, ‘the question [here] is whether courts defer to the justifications provided by the [parties to the dispute] or rather undertake an entirely independent review of the measures at issue’¹⁵³. The intensity of review, though a separate entity, thus influences the standard of review in that a deferential breed of the former will dull the edge of the latter.¹⁵⁴ Other articulations of the issue are whether or not a certain provision may be considered “self-judging”, and to what extent the state party is awarded a “margin of appreciation” by the tribunal.

¹⁵¹ See Engle, E., *The History of the General Principle of Proportionality: An Overview* part II section B.

¹⁵² In the context of EU law, see Craig, P., *EU Administrative Law* part II chapter 18 section 6 subsection A.

¹⁵³ Andenæs, M. and Zleptnig, S., *Proportionality: WTO Law in Comparative Perspective* chapter III page 392.

¹⁵⁴ See Shany, Y., *Toward a General Margin of Appreciation Doctrine in International Law?* part 1 section A page 911.

In any case, the level of intensity to review to be expected applied in any specific case is not always obvious up front. While some tribunals, notably the ECHR with its margin of appreciation standard,¹⁵⁵ have developed fairly sophisticated instruments for dealing with the question, others, like the WTO tribunals and their objective assessment standard,¹⁵⁶ seem to have taken a somewhat vaguer position on the issue. As for the tribunals arbitrating under international investment law, they presently do not appear to utilize any very common standard for the intensity of review at all.¹⁵⁷ To complicate the matter even further, a tribunal might conceivably address the intensity of review but implicitly, and it might also find it prudent exercise different intensity levels at the different stages of the applicable standard of review framework.

Be it implicit or explicit, deferential or rigorous, fixed or differentiated, the intensity of review is nevertheless an integral and inherent part of any balancing procedure. While the standard of review is the framework governing the latter, the intensity of review is a freestanding concept that applies to the actual balancing process at all stages of the framework.¹⁵⁸ Though structurally independent concepts, the intensity of review and standard of review do, as seen, influence each other, prompting the sentiment that for the one to consistently contribute to certainty and stability in a balancing process, the other needs to be adequately clarified. In terms of the impact of the proportionality standard on international investment law, this might potentially constitute an issue since no common standard for the intensity of review, as mentioned, herein exists. Some commentators argue

¹⁵⁵ See for instance Brownlie, I., *Principles of Public International Law 7th Edition* part IX chapter 25 section 13 subsection (A).

¹⁵⁶ See for instance Ehlermann, C. D. and Lockhart, N., *Standard of Review in WTO Law*.

¹⁵⁷ See Burke-White, W. W. and von Standen, A., *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties* part VI especially pages 368-370.

¹⁵⁸ Within the context of EU law, see Craig, P., *EU Administrative Law* part II chapter 17 section 2 page 657 and chapter 18 section 6. Note, as material illustrating the difference between a standard of review question and an intensity of review question, Craig's reasoning on differing intensity of review levels being applied to the proportionality framework within EU law when reviewing a challenge to EU Community actions relative to when reviewing a challenge to Member State actions (chapter 17 versus chapter 18).

for the use of the margin of appreciation standard of the ECHR to amend this issue.¹⁵⁹

In other words; balancing within international investment law may presently be conceptually assimilated with a mathematical equation containing two unknowns: One in the form of the standard of review question and one in the form of the intensity of review question. To be able to solve such an equation, the unknowns must be pegged down separately since they otherwise would influence each other and produce a range of solutions rather than a single one. A tribunal, however, is necessarily unable to utilize a range of different solutions when faced with one single balancing situation. Thus, the unknowns must be untangled and handled up front. The aim of this thesis is to peg down the unknown known as standard of review. The second unknown, in the form of intensity of review, is a different question that will not be further tackled herein beyond being indicated as an issue any arbitration tribunal conducting a balancing procedure necessarily also must face.

3.2 Diffusion

A number of different jurisdictions and legal disciplines have so far embraced proportionality analysis as the preferred standard of review to be utilized in situations where balancing is merited. This section will provide a brief overview of the diffusion of the concept, indicating the level of commitment proportionality is awarded throughout both international and municipal law. Note that proportionality in the specific context of international investment law is discussed in section 3.3 and chapter 5.

3.2.1 *The European Convention on Human Rights*

The ECHR has been in force since 1953, and establishes a basic catalogue of human rights that its parties are bound to uphold within their jurisdiction. It has proved to be a

¹⁵⁹ See Burke-White, W. W. and von Standen, A., *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties* part X.

remarkably effective and progressive instrument, regularly upgraded through revisions and directly administered by the European Court of Human Rights.¹⁶⁰ Any citizen of the mentioned parties to the convention may, provided he has exhausted all national remedies, make an appeal directly to the Court in the event of a possible breach of any ECHR standard affecting him.¹⁶¹ Some of the articles of the ECHR (articles 8-11), however, are qualified by a necessity clause holding that the state parties may interfere with the right in question when such interference is deemed necessary for certain explicit reasons.¹⁶² This forces a balancing act on any tribunal reviewing any one of those articles.

In the event of the Court examining the necessity defence of a state party under articles 8-11 of the ECHR, it will revert to the proportionality standard in the balancing procedure, complimented by the margin of appreciation approach to the intensity of review question.¹⁶³ The initial source of this doctrine was the *Handyside v the UK* case, but subsequent rulings have refined and explained it. Setting an authoritative example for the parties to the ECHR, the Court has thus been a driving force behind the diffusion of proportionality as a recognized legal principle across Europe.¹⁶⁴

3.2.2 EU law

Initiated by the Treaty of Rome of 1959, the first pillar of the EU, often referred to as the European Community (EC) pillar, laid down the foundation for the common market of Europe by sketching out a blueprint based on a ban on discrimination.¹⁶⁵ The ECJ have

¹⁶⁰ See Sweet, A. S. and Mathews, J., *Proportionality Balancing and Global Constitutionalism* part IV section B subsection 2.

¹⁶¹ In accordance with the ECHR protocol 11 amendments to articles 34 and 35.

¹⁶² See ECHR paragraph 2 of articles 8-11.

¹⁶³ See Sweet, A. S. and Mathews, J., *Proportionality Balancing and Global Constitutionalism* part IV section B subsection 2 pages 149-150.

¹⁶⁴ See in general Keller, H. (ed.) and Sweet, A. S. (ed.), *A Europe of Rights: The Impact of the ECHR On National Legal Systems*, especially part III chapter 11 pages 698-701 and Craig, P., *EU Administrative Law* part II chapter 17 section 2.

¹⁶⁵ See Sweet, A. S. and Mathews, J., *Proportionality Balancing and Global Constitutionalism* part IV section

subsequently developed from the ban the principle of proportionality as a basic legal tenet when dealing with any kind of balancing procedure within EU law.¹⁶⁶ Indeed, it would seem that there presently exists a certain consensus among the authorities on the latter that proportionality is the legal framework to be used whenever a standard of review is required.¹⁶⁷

As was the case with ECHR law, the proportionality standard is perhaps most discernable in EU law through cases where derogation is the issue at hand. According to article 30 of the Treaty of Rome, for example, a member state may derogate from the principle of free movement of goods laid down in article 28 only for certain explicit reasons. In its use of proportionality as the procedural method for approaching the balancing thereby required, the ECJ further promotes the diffusion of proportionality across Europe in a manner not dissimilar to that of the European Court of Human Rights.

3.2.3 WTO law

Proportionality as a required, or even preferred, standard of review appear less established in the context of WTO law than it did in the context of both ECHR law and EU law: Contemporary commentators seem positioned both for and against the notion,¹⁶⁸ and neither WTO panels nor the Appellate Body have yet conjured up any judgement definitely settling the matter.¹⁶⁹ The issue is particularly acute in relation to public policy exceptions such as the GATT article XX and the General Agreement on Trade in Services (GATS) article XIV. These allow for derogation from the obligations of the treaties if such is deemed necessary for, or relates to, certain explicit reasons, thus forcing a balancing

B subsection 1 page 140.

¹⁶⁶ See for instance the *Schraeder v Hauptzollamt Gronau* case page 2269 in which the ECJ held that ‘the principle of proportionality is one of the general principles of Community law’.

¹⁶⁷ See Ortega, L. (ed.) *Studies On European Public Law: The Europeanization of Public Law and the European Constitution* chapter II page 37.

¹⁶⁸ For the position see Hilf, M., *Power, Rules and Principles: Which Orientation for WTO/GATT Law?* page 120, against it see Desmedt, A., *Proportionality in WTO Law*.

¹⁶⁹ See Van den Bossche, P., *Looking for Proportionality in WTO Law* part 1.

operation on any tribunal considering the provisions.

The somewhat vague position of proportionality in WTO law is probably at least partly due to the Appellate Body's tendency to mix the necessity and proportionality *stricto sensu* tests into one jumbled discussion.¹⁷⁰ The operative decision here would appear to be the *Korea – Various Measures on Beef* case,¹⁷¹ and subsequent rulings seem to more or less follow the pattern there sketched out.¹⁷² It may be, however, that the Appellate Body in the *Brazil – Measures Affecting Imports of Retreaded Tyres* case in stating that '[the measure in question's] contribution to the achievement of the objective must be material, not merely marginal or significant, especially if [it] is as trade restrictive as an import ban',¹⁷³ takes a small step further towards a standard of review more formally based on the proportionality framework. This thesis, concerning itself mainly with proportionality in international investment law, will not further address that question though, at least not beyond noting that even though its specific function not is completely clarified as of yet, proportionality at least does not seem to be principally excluded from the sphere of WTO law.¹⁷⁴

3.2.4 Public international law

Also within the realm of public international law has proportionality been on the agenda. A standard of review is hereunder required applied to a range of issues affecting the relationship between states, and proportionality holds, as just shown, a fairly prominent international position among the possible alternatives. An example of a public international

¹⁷⁰ More specifically, proportionality *stricto sensu* argumentation is typically imported into the necessity evaluation by way of the reasonability component of the necessity test. See *ibid.* part 6.

¹⁷¹ See *Korea – Various Measures on Beef* paragraphs 164 onward.

¹⁷² See for instance *US – Gambling* paragraphs 306-307.

¹⁷³ *Brazil – Measures Affecting Imports of Retreaded Tyres* paragraph 210.

¹⁷⁴ For a more in-depth analysis to the same effect, see Andenæs, M. and Zleptnig, S., *Proportionality: WTO Law in Comparative Perspective*, in particular chapter VI part A section 4. For a critique of the current WTO jurisprudence on the standard of review applied to public policy exceptions, see Kapterian, G., *A Critique of the WTO Jurisprudence on 'Necessity'*.

law area in need of a standard of review is the law of countermeasures.¹⁷⁵ Indicatively entitled ‘Proportionality’, article 51 of the International Law Commission (ILC) Draft Articles on Responsibility of States for Internationally Wrongful Acts states that ‘countermeasures must be commensurate with the injury suffered, taking into account the gravity of the international wrongful act and the right in question’¹⁷⁶. The wording indicates that a certain balancing procedure is required in the context of reviewing whether the countermeasure under scrutiny was wrongful, and also that qualitative factors should be taken into account in this review. The latter position necessarily pushes it towards a proportionality *stricto sensu* analysis, and, by extension, the proportionality framework.¹⁷⁷ In other words; proportionality will be the preferred standard of review for a tribunal evaluating the legality of a countermeasure as it links the mean to the aim pursued and assesses the appropriateness of the aim relative to other norms, interests and values affected.¹⁷⁸ In the *Gabcíkovo-Nagymaros Project* case, the International Court of Justice (ICJ) affirmed this role of proportionality with regards to countermeasures,¹⁷⁹ and used the framework thereby established to assess the merits of that case.

Proportionality might also be said to play a role in many other areas of public international law, but to here appraise that entire contextual field would push this thesis far beyond its scope. Suffice it to conclude that albeit definitely applicable therein, ‘it is difficult to identify a coherent substantive content of proportionality across the whole range of public international law’¹⁸⁰. As was the case regarding WTO law, the concept is thus still pending some form of definite juridical acceptance as a fundamental principle of public international law similar to the one it enjoys under EU and ECHR law.

¹⁷⁵ See Franck, T. M., *On Proportionality of Countermeasures in International Law* parts II and III.

¹⁷⁶ The Draft Articles are commonly held to reflect customary international law; see Rosenstock, R. and Kaplan, M., *The Fifty-third Session of the International Law Commission* section I.

¹⁷⁷ See section 3.1.3 and chapter 6.

¹⁷⁸ See Cannizzaro, E., *The Role of Proportionality in the Law of International Countermeasures* part 6.

¹⁷⁹ See *Gabcíkovo-Nagymaros Project* paragraph 85.

¹⁸⁰ Andenæs, M. and Zleptnig, S., *Proportionality: WTO Law in Comparative Perspective*, in particular chapter VI page 398.

3.2.5 Municipal legislature

Although traces of it can be discerned as early as antiquity,¹⁸¹ the concept of proportionality is usually recognized as having been formally developed in late 19th century Germany.¹⁸² During the redrafting of the German Federal Republic in the aftermath of the Second World War, it was also recognized there as a constitutional principle.¹⁸³ Building on German law as well as the emerging case law of the European Court of Human Rights and later also of the ECJ,¹⁸⁴ the principle subsequently spread throughout the European countries, first among the countries of Continental law origins,¹⁸⁵ and then also finding its way into Common law traditions.¹⁸⁶ From there, proportionality has been further diffused across most effective systems of constitutional justice of the world, perhaps with the US as a partial exception.¹⁸⁷

Given the importance of the US in terms of cross-border investment outflow, a few specific notes on the approach to proportionality within US law are perhaps thereby merited. Due to its ambivalence towards balancing stemming from the fears discussed above in section 3.1, it would seem that the Supreme Court has developed a somewhat varied standard of review concept, elastic relative to the underlying right(s) discussed:¹⁸⁸ While some areas of law are subject to a fairly thorough standard of review similar to that of proportionality,¹⁸⁹ others only experience the light touch of rational basis testing.¹⁹⁰ In

¹⁸¹ See Engle, E., *The History of the General Principle of Proportionality: An Overview* part I.

¹⁸² See Sweet, A. S. and Mathews, J., *Proportionality Balancing and Global Constitutionalism* part III.

¹⁸³ Ibid. part III section B page 105.

¹⁸⁴ See sections 3.2.1 and 3.2.2.

¹⁸⁵ See Sadurski, W., *Rights Before Courts: A Study of Constitutional Courts in Post-communist States of Central and Eastern Europe* part II chapter 9 page 287.

¹⁸⁶ See Engle, E., *The History of the General Principle of Proportionality: An Overview* part II section B.

¹⁸⁷ See Sweet, A. S. and Mathews, J., *Proportionality Balancing and Global Constitutionalism* part I page 75.

¹⁸⁸ Ibid. part I page 79.

¹⁸⁹ An example would be the interstate commerce clause of the US Constitution article I § 8. See Andenæs, M. and Zleptnig, S., *Proportionality: WTO Law in Comparative Perspective* chapter V page 405.

¹⁹⁰ See Sweet, A. S. and Mathews, J., *All Things in Proportion?: American Rights Doctrine and the Problem of Balancing* part IV section A.

general it is thus problematic to draw any final conclusion as to the standing of proportionality in US law, the lack of which is casting a shadow over the status of proportionality in an international investment context due to the prominent juridical importance the US presently enjoys on the global stage.¹⁹¹

3.3 Proportionality versus international investment law

This section is but intended to roughly sketch out the current situation regarding proportionality in an investment law context. The more in-depth analysis of the topic is found in chapter 5 below. Section 3.3.1 may therefore be viewed as a foreshadowing of chapter 5, sketching out the framework of and setting the scene for the main discourse this thesis concerns itself with.

3.3.1 A snapshot

Though still fairly unmapped, the role of proportionality in international investment law recently became somewhat less diffuse through the legal aftermath of the 2001 Argentine financial crisis. Together with the earlier *Tecmed v Mexico* ICSID arbitration of 2003, the (so far) 8 arbitrations leading out of the Argentine case complex comprise an emerging body of case law touching upon the matter. The cases referred to are: *CMS v Argentina*, *LG&E v Argentina*, *Enron v Argentina*, *Sempra v Argentina*, *Continental Casualty v Argentina* and the ICSID Annulment Committee rulings pursuant to the *CMS*, *Sempra* and *Enron* awards. Some statements about the issue are also found in the Annulment Committee ruling pursuant to the *Vivendi II* award.

The *Tecmed* award will be further explored in section 5.5.2. As for the cited cases involving Argentina, they all derive from a common set of facts. A few notes on that case complex are at this point merited to set the stage for the dissection of its functional content throughout chapter 5: During the 1990s, Argentina endeavoured democratize and open up

¹⁹¹ For a general comparison between proportionality and the US approach to balancing see Porat, I. and Cohen-Eliya, M., *American Balancing and German Proportionality: The Historical Origins*.

its economy by, among other things, embrace the BIT regime, ratify the ICSID Convention and privatize an extensive portfolio of State-run companies.¹⁹² The country also implemented a range of legislative reforms to attract foreign investments; including pegging its currency to the dollar and promising that capital would be allowed to flow freely across its borders.¹⁹³ Then disaster struck in 2001 by way of a national financial crisis precipitated by heavy budget deficits, balance of payment discrepancies and mounting foreign debt.¹⁹⁴ To meet that crisis, the Argentine government 'adopted a number of measures to stabilize the economy and restore political confidence. Among these efforts was a significant devaluation of the peso through the termination of the currency board which had pegged the peso to the US dollar, the pesification of all financial obligations, and the effective freezing of all bank accounts through a series of measures known collectively as the *Corralito*'¹⁹⁵.

Naturally, foreign investors were bound sustain losses as a consequence of the government's actions. More specifically, CMS, Enron, Sempra, LG&E and Continental Casualty Company all lost their right to calculate tariffs in US dollars and then convert them to pesos at the prevailing exchange rate.¹⁹⁶ They subsequently initiated arbitration proceedings before ICSID tribunals on account of Argentina allegedly having breached the US-Argentina BIT by effectuating the capital control regime and thereby (among other

¹⁹² See Sweet, A. S., *Investor-State Arbitration: Proportionality's New Frontier* part IV page 69.

¹⁹³ See Kurtz, J., *Adjudging the Exceptional at International Investment Law: Security, Public Order and Financial Crisis* part II section A pages 330-331.

¹⁹⁴ In part, this was caused by a fall in global price levels of key Argentine export products at the same time as the dollar experienced an ascending trend relative to the other major international currencies and Brazil, Argentina's principal trading partner, devaluated its currency. See in general Epstein, E. (ed.) and Pion-Berlin, D. (ed.), *Broken Promises? The Argentine Crisis and Argentine Democracy* part II chapter 4.

¹⁹⁵ Burke-White, W. W. and von Standen, A., *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties* part I pages 309-310.

¹⁹⁶ See *CMS v Argentina* paragraphs 59-73, *Enron v Argentina* paragraphs 41-46 and 62-79, *Sempra v Argentina* paragraphs 93, 100-105 and 116-121, *LG&E v Argentina* paragraphs 34-71 and *Continental Casualty v Argentina* paragraphs 100-128 and 137-147.

things) indirectly expropriated foreign property.¹⁹⁷ As shall be further discussed below in chapter 5, Argentina defended itself against those claims by in various ways asserting that its conduct was justified under the BIT as a consequence of the severe crisis situation the country had been faced with.

Taking a step back from the concrete exemplification provided by the Argentine case complex into more theoretical terrain, it is thus discernable that proportionality may enter the investment realm at some specific choke points. Most relevant, in terms of availability of case law, is through the evaluation of so-called Non-Precluding Measure (NPM) clauses of BITs, MITs and investment contracts. All of the Argentine cases fall into this category.¹⁹⁸ A NPM clause ‘limits the applicability of investor protection under [a specific BIT, MIT or investment contract] in exceptional circumstances’¹⁹⁹. It typically excludes a state breach of the BIT under qualified conditions. Proportionality, as a standard of review, may be utilized when assessing the qualification requirement of any such condition.

Second, proportionality might, similar to its function in the evaluation of NPM clauses, be considered the standard of review to be utilized in the evaluation of any claim based on the necessity defence of article 25 of the ILC Draft Articles on Responsibility of States for Internationally Wrongful Acts. A state, faced with an investment claim, might turn to this one as a NPM-like response to escape liability it otherwise would procure. Argentina claimed article 25 of the Draft Articles applicable in this way in all of the above-mentioned cases.²⁰⁰ The relationship between NPM clauses of BITs, MITs and investment contracts and article 25 of the Draft Articles will be further discussed below in section 5.3.

Third, proportionality may conceivably be a procedural factor in evaluating whether

¹⁹⁷ See Kurtz, J., *Adjudging the Exceptional at International Investment Law: Security, Public Order and Financial Crisis* part II section B.

¹⁹⁸ See Sweet, A. S., *Investor-State Arbitration: Proportionality's New Frontier* part IV pages 69-70.

¹⁹⁹ Burke-White, W. W. and von Standen, A., *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties* part I page 311.

²⁰⁰ See Alvarez, J. E. and Khamsi, K., *The Argentine Crisis and Foreign Investors: A Glimpse Into the Heart of the Investment Regime* part II section B.

the oft-cited fair and equitable treatment standard has been breached.²⁰¹ The function of this one is basically to fill any legal gaps regarding an investment relation, securing the level of investment protection intended by the legal instrument in question.²⁰² In this sense the principle upholds the goal of legal stability and predictability. To assess whether or not the host state has treated the investor in a fair and equitable manner, it may be prudent for the tribunal to take the entirety of the factual situation into account.²⁰³ If so, the question of whether the state actions are to be considered fair and equitable in relation to the affected interests of the investor necessarily must be relative to any opposing norms, interests and values at issue. This invites a balancing operation that in turn, as seen, must rely on some standard of review, for instance proportionality.

Finally, the proportionality framework might also be utilized as the operative procedural framework in any other situation requiring a trade-off between competing norms, interests and values. In the *Tecmed v Mexico* case for instance, the tribunal employed a proportionality *stricto sensu* test in evaluating whether a measure was to be considered expropriatory.²⁰⁴ It had to determine whether a particular article of the BIT between Spain and Mexico covered a certain government decision. Balancing the interests of Tecmed against the interests of Mexico under the proportionality *stricto sensu* test turned out to be a key component of this evaluation.²⁰⁵ Similar sentiments may in principle also be forwarded in any other balancing situation under international investment law.

In any case, the crucial question at this point is whether and to what extent the principle of proportionality actually is utilized by tribunals facing any of the 4 situations

²⁰¹ The fair and equitable treatment standard is often formally embedded in a BIT, MIT or investment contract clause. See for instance the 2004 US Model BIT article 5. Whether it also is a part of customary international law, for instance the minimum standards of protection of aliens, seems to be a somewhat debated issue. For a fairly in depth review of this question, see Tudor, I., *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment* chapter 2.

²⁰² See Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter VII part 1 section C.

²⁰³ See Tudor, I., *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment* chapter 3 part 3.3.1 sections iii and iv.

²⁰⁴ See *Tecmed v Mexico* paragraph 122 and onward.

²⁰⁵ See section 5.5.2 below.

now sketched out. This is the main issue of this thesis, and will be thoroughly discussed in section 5 below. The structure of that chapter is based on the four lays of applicability just identified: Section 5.1 covers NPM clauses, section 5.2 covers the necessity defence of the Draft Articles of State Responsibility, section 5.4 covers the fair and equitable treatment standard, and section 5.5 covers proportionality in all other contexts.

3.4 Environmental considerations

Chapter 5 will utilize a constructed investment law case, outlined in chapter 4, to illustrate its argumentation. The case is centred on environmental issues, whereupon a few notes on how these may enter a balancing context are merited in advance.

Typically, the environment is considered a so-called public good. Since no one per definition can be excluded from the consumption of such goods, their markets often fail due to free riding, preference misevaluation and inability to appropriate an adequate return.²⁰⁶ Public goods may be quite valuable to the well-being and development of a society, however. Therefore, governments often find it prudent to address the mentioned market failures by regulating the markets of public goods more or less extensively. That regulation may in turn influence the rights and duties of other entities operating within the government's sphere of jurisdiction, though. If the government's public good regulation affects them negatively, such entities may try to initiate legal actions in order to halt it.

A court or tribunal faced with an action of the latter variety does, if the legal circumstances in question concern principles rather than rules, often find itself confronted with a balancing situation. In the case of environmental regulation, environmental considerations clash with the (often economic) rights and interests of the affected non-government entities. In terms of international investment law, a typical scenario would involve government environmental regulation limiting foreign investor rights as established by a BIT, MIT or investment contract. The opposite scenario, under which it is the investor who asserts environmental considerations to support his position, is rather unlikely.

²⁰⁶ See Veljanovski, C., *Economic Principles of Law* chapter 2 page 40.

4 The scenario

To make this thesis less of an overly theoretical exercise, an empirical scenario will in chapter 5 and beyond be used to illustrate the main argumentation. Chapter 4 will sketch out this scenario without getting lost in its details. Section 4.1 introduces the parties to the fictional dispute, and section 4.2 sketches out the juridical predicament faced. The information presented in this chapter may later be altered if so is required in order to illuminate a certain argument or position. Any alterations will be explicitly made clear as such at that point though. Unless something else subsequently is noted, the scenario returns to its initial configuration after the illumination is complete.

4.1 The parties

This section introduces the parties to the constructed investment law case that chapter 5 will utilize as illustrative material. The state party to the dispute is Xanadu, and the investor will be known as the Resources Development Administration.

4.1.1 Xanadu

The khanate of Xanadu²⁰⁷ is a sparsely populated independent nation located in a mountainous valley of central Asia, and known for its abundant deposits of various natural resources. It additionally possesses scenic environs made up of fertile grounds, tree-filled gardens, ancient forests and green hills. The nation's identity lies chiefly in its image as a place of untouched natural beauty, and a number of species of both flora and fauna are unique to its domain. Biologists have theorized that the exceptional environmental characteristics of Xanadu are due to a vast network of underground rivers and seas that provide the vegetation of the valley with an abundance of pristine and mineral rich water.

²⁰⁷ Inspired by the poem *Kubla Khan* or *A Vision in a Dream* by Coleridge, S. T. (1797).

4.1.2 *The Resources Development Administration*

The Resources Development Administration (RDA)²⁰⁸ is an American corporation specializing in the extraction of rare earth minerals, wholly owned by American investors. It operates across the globe, and is a large and well-known corporate entity with historically a decent, though not unbreakable, financial backbone. The recent global financial crisis, however, led to a slump in the general demand for the minerals the RDA extracts and refines, in turn negatively affecting its profit margins. Any further unexpected financial stress could thus cause severe existential problems for the company.

4.2 The dispute

This section will sketch out the juridical predicament faced, as well as the course of events leading up to the arbitration proceedings.

4.2.1 *A conflict of interests*

At the beginning of the 21st century, a deposit of the mineral known as unobtainium was discovered in the sediments of Xanadu. Unobtainium may be refined into a metal with the properties of a so-called superconductor, and thus fetches ridiculous prices on the world market. The RDA was awarded the right of extraction of Xanaduian unobtainium, and subsequently invested heavily in machinery to this purpose, as well as in a refinery and in the Xanaduian infrastructure. On its part, the Xanaduian government pledged to not interfere with the RDA's operations in any way, and to consult with the RDA before changing any municipal legislature which might affect them.

A few years after the RDA began its extraction and refining operations, some adverse effects were being observed on the environment of Xanadu. First, the trees of its famed gardens turned less incense bearing than earlier, and then the flora in general started withering. As a result, several species of plants, insects and animals were fast approaching the brink of extinction. Investigations as to the cause of the devastation were conducted,

²⁰⁸ Inspired by the motion picture *Avatar* by Cameron, J. and 20th Century Fox (2009).

providing the results that the RDA's extraction of the unobtanium deposit was polluting a high-lying underground water spring, in turn affecting the entire network of underground rivers and lakes. Further examinations revealed that it unfortunately would be functionally impossible to extract the unobtanium without continuing the pollution of the spring, at least unless some ridiculously costly cleansing measures were implemented.

The Xanaduian government, fearing being blamed for an environmental catastrophe and being pressured by a number of international environmental organizations, immediately effectuated a ban on extraction of unobtanium, thereby instantaneously halting the RDA's operations. The RDA, as a result, experienced a sudden decline in operational profits and also had to take a heavy financial loss in that its right of extraction of Xanaduian unobtanium abruptly became virtually valueless. The company was fast approaching the brink of bankruptcy.

As the investors behind the RDA saw their values evaporating, mediation between the RDA and the Xanaduian government was tried initiated. The government absolutely declined to in any way adjust its ban on unobtanium extraction however, citing that its concern for Xanadu's environment was paramount. As a result, the RDA and its investors began preparing for legal action against Xanadu on the basis of international investment law.

4.2.2 The issue under international investment law

Between Xanadu and the USA, a BIT was, and had been at the time of the RDA's investment, in place. The RDA had considered this one effectual enough to not press for a specific investment contract during its initial negotiations with the Xanaduian government concerning the extraction of the unobtanium.²⁰⁹ Furthermore, Xanadu was also a party to

²⁰⁹ Since the discussions of chapter 5 is based on the constructed investment case of chapter 4, this necessarily leads to the main argumentation of this thesis relating more to BITs (and MITs) than investment contracts. This is an intentional functional choice as a consequence of the standard of review debate within international investment law currently seeming to be more or less exclusively situated in a BIT (and MIT) context. It is probable that several of the arguments forwarded in relation to BITs (and MITs) have considerable

the ICSID convention. The RDA and its shareholders thus found it prudent to initiate an ICSID arbitration based on the provisions of the US-Xanadu BIT.

The claim advanced relied on article 6 of that BIT, an article stating that:²¹⁰

Article 6: Expropriation and Compensation

Neither Party may expropriate or nationalize a covered investment either directly or indirectly through measures equivalent to expropriation or nationalization, except:

- (a) for a public purpose;
- (b) in a non-discriminatory manner;
- (c) on payment of prompt, adequate, and effective compensation; and
- (d) in accordance with due process of law

Holding that the ban on extraction of unobtainium constituted a measure equivalent to indirect expropriation, the RDA and its investors claimed to be entitled to full compensation in accordance with alternative C of this provision. Furthermore, they held that the Xanaduian government had breached the fair and equitable treatment standard of article 5 of the BIT. Article 5 stated that:²¹¹

Article 5: Minimum Standard of Treatment

Each Party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security. If an investor of a Party suffers a loss in the territory of the other Party resulting from a breach of the abovementioned standards, the latter Party shall provide the investor restitution, compensation, or both, as appropriate, for such loss. Any compensation shall be prompt, adequate, and effective.

Compensation in accordance with this article was claimed on the basis of the Xanaduian government's failure to provide a stable legal and business environment; thereby failing to protect the RDA's legitimate interests, and due to the government's failure to act in accordance with its pledges of non-interference and consultation.

Xanadu did not challenge the claim that the ban on extraction of unobtainium

transfusion value to an investment contract context as well though.

²¹⁰ Based on article 6 paragraph 1 of the 2004 US Model BIT.

²¹¹ Based on article 5 paragraph 1 and 5 of the 2004 US Model BIT.

constituted an indirect expropriation in accordance with article 6 of the BIT. It did however, assert that no compensation was due since the measure in question was covered by both the NPM clause of article 18 alternative 2 of the BIT, and the customary necessity defence based on article 25 of the ILC Draft Articles on Responsibility of States for Internationally Wrongful Acts. Article 18 of the BIT stated that:²¹²

Article 18: Essential Security

Nothing in this Treaty shall be construed:

1. to require a Party to furnish or allow access to any information the disclosure of which it determines to be contrary to its essential security interests; or
2. to preclude a Party from applying measures necessary for the maintenance of public order, the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests or human, animal or plant life or health.

Article 25 of the Draft Articles stated that:

Article 25: Necessity

Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:

- (a) is the only way for the State to safeguard an essential interest against a grave and imminent peril; and
- (b) does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole.

In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:

- (a) the international obligation in question excludes the possibility of invoking necessity; or
- (b) the State has contributed to the situation of necessity.

Regarding the claim that it had breached the fair and equitable treatment standard of article 5 of the BIT, Xanadu alleged that the standard should be assessed in the context of the situation. Viewed against the backdrop of preventing a possible environmental catastrophe, it therefore could not be considered breached.

²¹² Based on article 18 of the 2004 US Model BIT and article 10 of the 2003 Canadian model FIPA.

4.2.3 Further assumptions

In order to ensure that the scenario now presented stays within the context this thesis aims at assessing (that of proportionality in international investment law) some further assumptions about the legal procedure between Xanadu and the RDA have to be made: First, it shall be assumed that the ban on unobtainium extraction falls within the sphere of permissible objectives stated in article 18 of the BIT, thus making the question of whether or not the measure was “necessary” the only issue to be evaluated. Given the wording of alternative 2 of this provision, such an assumption is probably not too preposterous.

Furthermore, it shall also be assumed that the ban on unobtainium extraction fulfils the similar requirement of scope of the first paragraph of article 25 of the Draft Articles (“grave and immediate peril”), and that the exceptions of the second paragraph do not come into effect.²¹³

Finally, article 18 of the BIT shall be interpreted to mean that it absolves Xanadu from the duty to pay compensation in the event of the government breaching article 6. There seems to be some theoretical disagreement as to whether article 18 of the 2004 US Model BIT does so.²¹⁴ In general, all assumptions to the effect of making the balancing procedures inherent in article 5 and 18 of the BIT and article 25 of the Draft Articles the primary issues to be debated, eliminating all other possible sources of juridical conflict, are, and should be, made.

²¹³ Note that the ICJ *Gabcikovo-Nagymaros Project* case paragraphs 39-41 would seem to affirm that environmental consideration may be invoked under article 25 of the Draft Articles.

²¹⁴ It is argued in Alvarez, J. E. and Khamsi, K., *The Argentine Crisis and Foreign Investors: A Glimpse Into the Heart of the Investment Regime* chapter III part E that it does not, while in Burke-White, W. W. and von Standen, A., *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties* chapter VII part A it is argued that it does.

5 Proportionality in the scenario context

Having roughly sketched out both the sphere of international investment law in chapter 2 and the concept of proportionality in chapter 3, time has now come to combine the quantities by assessing the merits of proportionality within international investment law. As was indicated in section 3.3, the question is to what extent the proportionality framework is, and for that matter should be, utilized by international investment law arbitration tribunals faced with situations where balancing of competing principles is the issue. Section 3.3 also indicated four possible lays of applicability. This chapter will follow the outline there advanced in its analysis of proportionality's diffusion, or lack thereof, throughout the law governing international investments: First, the preclusion of expropriation context of NPM clauses will be discussed in section 5.1. Then, in section 5.2, the customary necessity defence of the Draft Articles on State Responsibility will be tackled. In section 5.3, as a necessary, slight digression, the somewhat problematic relationship between the standard of review question in a NPM context and the standard of review question in a customary necessity defence context will be explored. Section 5.4 will return to the initial framework by discussing proportionality under the fair and equitable treatment standard, while section 5.5 seals the analysis by reviewing its significance throughout the rest of the international investment law. The scenario outlined in chapter 4 will be utilized as a backdrop for the discussion under all sections.

5.1 Preclusion of liability

Xanadu claims that the NPM clause within article 18 second alternative of the US-Xanadu BIT precludes any liability the country otherwise would have procured by its ban on unobtanium extraction. Since the permissible objectives requirement of this provision is presumed fulfilled, the ICSID tribunal assessing the case thus only has to establish whether Xanadu's action can be deemed to have been "necessary for" achieving that objective. The

question is how this should be done. First paragraph of article 31 of the Vienna Convention indicates that a natural starting point for such a discussion might be the wording of the BIT. Section 5.1.1 will commence from that position in articulating a few general remarks on balancing within an NPM clause context. Section 5.1.2 will subsequently present the alternative standards of review that might be utilized by the tribunal, and section 5.1.3 will indicate which of them currently may be deemed the better supported by the instrumental sources of international investment law. Section 5.1.4 will finally round off the NPM clause standard of review analysis by evaluating proportionality's potential within this context on a more fundamental level.

5.1.1 The nexus requirement

Through the wording “necessary for”, article 18 of the US-Xanadu BIT requires a link between the measure adopted by the state and the permissible objectives sought reached. In other words, the ban on unobtainium extraction must in some way be causally connected to the protection of animal or plant life. The articulation of this condition has in theory often been termed “the nexus requirement”.²¹⁵ The nexus requirement may be paraphrased differently in different NPM contexts and within differing juridical instruments. “Necessary for” or “necessary to” are perhaps the most common terminology,²¹⁶ but alternatives are abundant.²¹⁷ Also, BITs or investment contracts in other languages than English may contain NPM clauses with nexus requirements deviating from the “necessary for” terminology as a function of inaccurate translations due to linguistic inconsistency.²¹⁸ The point is in any case that the nexus may be articulated differently, and that this might,

²¹⁵ See Burke-White, W. W. and von Standen, A., *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties* part V section B subsection 1.

²¹⁶ See for example the 2004 US Model BIT article 18 and the 2003 Canadian Model FIPA article 10.

²¹⁷ The 2007 Norwegian Draft Model BIT article 12 uses “appropriate for” for instance.

²¹⁸ See Burke-White, W. W. and von Standen, A., *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties* part V page 342.

through the methodology indicated by section 2.3 above, lead to differing standards of review being utilized in the evaluation of differently worded NPM clauses.

In fact, even the standards of review utilized under similarly worded NPM clauses may differ: Since the wording of a BIT (or MIT or investment contract) provision is but one factor of interpretation,²¹⁹ the varying mix-up of sources of law in each specific investment case may very well lead to differing standards of review being utilized even between cases of similarly worded nexuses. However, on the basis of the Vienna Convention article 31 first paragraph, it may be argued that similar wording of articles with similar function contained in instruments with similar object and purpose should in general be interpreted similarly. In light of the general legal aim of consistency and predictability, this argumentation would appear to hold a certain intrinsic persuasiveness. Note, however, that no tribunal to date has explored the issue. Also, since each BIT, MIT and investment contract in essence is self-contained; the formal interpretative starting point must in any case be itself, whereas parallels to other investment law awards, however strong, are factors whose importance is based on persuasiveness rather than precedence.²²⁰ Nevertheless, lacking any other formal interpretive articulations, persuasiveness seems better than nothing, whereupon it may be argued that similarly worded NPM clauses perhaps should be assumed to refer to similar standards of review, at least unless something entirely different may be inferred from other interpretive factors.

Situating a further discussion of that problem on the sideline for the time being, and moving back into the standard “necessary for” terminology however, the questions still remains which standard of review to utilize in evaluating the nexus. The US-Xanadu BIT does, like most other BITs presently out there, not explicitly regulate this question. One central issue that thereby has to be faced is how the “necessary for”-term should be interpreted in this respect. Some alternatives, as will be indicated in section 5.1.2 below, exist, but the very first matter that needs to be clarified is whether the wording of an NPM clause does, and for that matter should, influence the standard of review evaluation at all.

Despite the wording of article 31, first paragraph of the Vienna Convention, the

²¹⁹ See section 2.3.

²²⁰ See *ibid.*

affirmation that the terminology of the nexus requirement may influence the standard of review to be utilized by anyone reviewing the requirement is perhaps somewhat less obvious than it initially would appear: As has already been noted, the standard of review is but the framework governing the juridical-analytical operation of balancing, while the nexus requirement is, in this case, the actual issue under review. To let the latter influence the former may thus seem a bit like a logical fallacy in that a factor of an equation always is logically separate from, and may thus not alter, the morphology the equation. Furthermore, to allow the object under review to affect the review process may lead to less legal predictability and consistency since it in such situations would be harder to discern one's legal position up front: Juridical terrain in which multiple, interlinked determinants modify and alter one and other is obviously harder to map out than topography dependant on but one factor. Nevertheless, the wording of the nexus requirement under scrutiny is usually the fixed point to where an analysis of which standard of review to be utilized is anchored, simply because no formally authoritative articulations are elsewhere found. Note in this respect also article 42 of the ICSID Convention which states that that 'the tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties'. The nexus requirement is thus probably the closest the US-Xanadu ICSID tribunal may get to such a rule relating to which standard of review it is to utilize in that its wording may indicate the direction of the parties' intention(s).

The latter topic is also closely tied to the issue of what authority the mentioned tribunal should exercise relative to the competence of the Xanadu to arrange its own internal affairs. This one was discussed in section 3.1.4 under the heading "intensity of review". An investment tribunal arbitrating under a strict intensity of review would appear freer to utilize the standard of review of its own choice than would a more deferential tribunal. The former may thus heed the wording of the nexus requirement less than may the latter. Since however, as mentioned above, it does seem to be the case that neither ICSID tribunals nor any other of the international investment kind exercise any common intensity of review standard, the conclusion of the preceding paragraph appear to still hold sway in the aggregate: As no other common trend or fixed point exist, the wording of the nexus requirement does influence the standard of review, even though the particular intensity of

review in question to a certain degree may dictate the amplitude. Case law seems to implicitly affirm this statement.²²¹

Having thereby found that it in principle may influence the standard of review, the logical structure would at this point be to indicate the alternative interpretations that the nexus of article 18 of the US-Xanadu BIT may be subject to. This will be done in section 5.1.2 just below. One additional note is required before delving into such an analysis, however: Lacking a comprehensive body of international investment law NPM clause jurisprudence dealing with standards of review, and especially the proportionality standard, the following discussion will from time to time utilize arguments from WTO law. Though WTO law and international investment law formally are distinct juridical entities, their somewhat similar context and scope in terms of concerning the transfer of capital across national borderlines prompts a certain crossover of argumentation based on its causal persuasiveness. It should be stressed that such transfusion needs be tempered by the differences between the entities, however. In a preclusion of expropriation context for instance, a WTO NPM clause protects the state against the community while an investment law NPM clause protects it against a private party. Differing premises are thus at play. Pains must be taken to ensure that the implications of such nuances not are lost in the transfusion.

5.1.2 *The alternatives*

In theory, an unlimited number of possible ways to review the nexus are conceivable. In international law practice however, but four distinct alternatives have crystallized.²²²

²²¹ The wording of the nexus requirement is used as a starting point in both *Continental Casualty v Argentina* (see part VI section D subsection A) and *LG&E v Argentina* (see paragraph 205), the only two still unannulled awards discussing the NPM clause of a BIT.

²²² See Burke-White, W. W. and von Standen, A., *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties* part V section B subsection 1. Note that Trachtman, J. P., *Trade and ... Problems, Cost-Benefit Analysis and Subsidiarity* identifies six different standards of review along an axis perhaps slightly askew relative to the one considered in this thesis. The slight difference in content and terminology might be due to a somewhat

These are “choice-constrained validity”, “self-defence-reliant necessity evaluation”, “least restrictive means analysis” and “proportionality”.²²³ Each will now be briefly dissected in turn. Afterwards, a few notes on some standard of review alternatives based on (US) municipal law are merited.

Starting off with the “choice-constrained validity” standard, this one would appear to be, as shall be further discussed in section 5.2.1, the preferred standard for reviewing of the nexus requirement of the Draft Articles on State Responsibility article 25.²²⁴ The gist here is that “necessary for” is equated with a situation where the state measure under evaluation is the only available way to safeguard the interest in question.²²⁵ Choice-constrained validity thus transforms the nexus requirement into a rule (as opposed to a principle) since no balancing will be required: If other, otherwise lawful, measures conceivably were available, the measure in question was not necessary, if not, then it was.²²⁶ Under this interpretation it is doubtful whether Xanadu will be able to rely on its defence of necessity under article 18 of the BIT: Other possible measures to safeguard the environment were, albeit complex and costly, conceivable. It might for instance have been possible to create some sort of an immensely expensive underground water-purifying plant just downriver from the unobtainium mine. The choice-constrained validity standard will be further addressed in section 5.2.1.

The second standard of review alternative, above dubbed “self-defence-reliant

more theoretical approach to the standard of review question in Trachtman’s commentary than the one envisioned herein.

²²³ Note that the terms “choice-constrained validity” and “self-defence-reliant necessity evaluation” are terminological constructs presently unique to this thesis.

²²⁴ See Kurtz, J., *Adjudging the Exceptional at International Investment Law: Security, Public Order and Financial Crisis* part II section C page 338.

²²⁵ See International Law Commission, *Responsibility of States for Internationally Wrongful Acts* part 1 chapter V article 25 paragraph 15.

²²⁶ In practice, this equates into a situation where the nexus requirement almost never can be satisfied since there invariably exists alternative ways to react to any situation. This is especially true in cases of economic necessity, see Reinisch, A., *Necessity in International Investment Arbitration – An Unnecessary Split of Opinions in Recent ICSID Cases?* part III section B page 200.

necessity evaluation”, has crystallized out of ICJ case law on US treaties on Friendship, Commerce and Navigation.²²⁷ Here, a self-defence requirement is imported into the definition of necessity. In the *Oil Platforms* case for instance, the ICJ held that ‘the question of whether the measures taken were “necessary” overlaps with the question of their validity as acts of self-defence’²²⁸. The jurisprudence and results of the *Oil Platforms* and *Nicaragua* cases indicate that this standard of review is a strict one. In the case of Xanadu, the ban on unobtainium extraction evidently does not constitute an act of self-defence, and would thus not be precluded by article 18 of the BIT if self-defence-reliant necessity evaluation was to be deemed the standard of review applicable.

The third standard of review alternative, “least restrictive means analysis” (often otherwise termed “least restrictive alternative test”), is, in fact, at the outset a standard not very different from “proportionality”. In assessing the standard of review question under international investment law, some commentators nevertheless hold least restrictive means analysis to be inherently more suited than proportionality in terms of functionality within the peculiar sphere of this legal subject.²²⁹ The crucial distinction is that while proportionality encompasses a three-stage procedure ending up in a proportionality *stricto sensu* test,²³⁰ least restrictive means analysis places all emphasis on the first two of the stages, and especially on the necessity stage.²³¹ As seen however, several tribunals have jumbled the necessity test together with the proportionality *stricto sensu* test into one combined analysis, not only prompting the question of which standard of review they actually are utilizing, but also blurring the conceptual borderline between proportionality and least restrictive means analysis in general. At the international level, especially some

²²⁷ See Burke-White, W. W. and von Standen, A., *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties* part V section B subsection 1 page 344.

²²⁸ *Oils Platforms* paragraph 43. See in general also the *Nicaragua* case.

²²⁹ See Kurtz, J., *Adjudging the Exceptional at International Investment Law: Security, Public Order and Financial Crisis* part V section B subsection 3.

²³⁰ See section 3.1.

²³¹ See section 3.1.2.

WTO tribunals, whose standard of review still not is completely clarified,²³² have been known to blur the mentioned borderline in cases like *Korea – Various Measures on Beef*.²³³ Other WTO tribunals would seem to have applied least restrictive means analysis more cleanly though.²³⁴

Whether or not Xanadu would be able to defend its measure of indirect expropriation by relying on the NPM clause of article 18 under a nexus review based on least restrictive means analysis, is a somewhat open question: That the suitability stage of this analysis is fulfilled would appear to be fairly obvious since the ban on extraction definitely proved functional in stopping the pollution. The debatable issue however, is whether any other measure than the ban employed, achieving the same level of environmental protection but less restrictive on the RDA operation, could have been implemented instead (the necessity requirement).

As did the *Continental Casualty* tribunal,²³⁵ the Xanadu tribunal could perhaps, as a starting point for the assessment of this question, take a look at the WTO Appellate Body *Brazil – Measures Affecting Imports of Retreaded Tyres* award. This one states that ‘in order to determine whether a measure is "necessary" within the meaning of [the article in question], a panel must assess all the relevant factors, particularly the extent of the contribution to the achievement of a measure's objective [...], in the light of the importance of the interests or values at stake. If this analysis yields a preliminary conclusion that the measure is necessary, this result must be confirmed by comparing the measure with its possible alternatives, which may be less trade restrictive while providing an equivalent contribution to the achievement of the objective pursued’²³⁶. The crucial point to be noted is that only measures contributing to the protection of the Xanaduian environment at least as much as did the ban on unobtanium extraction thus may be deemed alternative.²³⁷

²³² See section 3.2.3.

²³³ See *Korea – Various Measures on Beef* paragraphs 159-172.

²³⁴ See for instance the *Thailand Cigarettes* case paragraph 75.

²³⁵ See *Continental Casualty* paragraph 193.

²³⁶ *Brazil – Measures Affecting Imports of Retreaded Tyres* paragraph 156.

²³⁷ See above under section 3.1.2, as well as Andenæs, M. and Zleptnig, S., *Proportionality: WTO Law in*

Furthermore, any such measure must also be reasonably available to Xanadu. The range of possible alternatives has thereby been severely cropped, but are there any left? Obviously, the rinsing alternative presented under the choice-constrained validity standard is not viable since the river is flowing underground and that measure thereby would be too costly for Xanadu to be considered reasonable. Other scenarios could possibly be constructed, but to settle the matter in the context of this thesis, it may be assumed that all of them would be deemed unreasonable. The NPM clause of article 18 of the BIT would hence exclude Xanadu from liability under a standard of review based on least restrictive means analysis.

The final standard of review alternative is “proportionality”.²³⁸ This standard has already been thoroughly reviewed above, and should therefore need no further introduction here. In the Xanadu case, the review of the first two stages of a proportionality analysis under article 18 of the BIT will mirror the one conducted under the least restrictive means analysis above. Finding that the ban on extraction of unobtainium probably could be deemed suitable and necessary is not the end of the story here, however. It must subsequently be assessed whether the ban (as a function of the environmental interests sought protected) was proportional, in the strict sense of the word, to the opposing norms, interests or values of the RDA thereby infringed. The Xanaduian government’s interests in a continued protection of Xanadu’s environment must, in other words, be balanced against the RDA’s interests of protecting its investments. It may be that the latter interests hold so much relative weight that the ban on extraction of unobtainium, though suitable and necessary, not can be considered proportional.

Comparative Perspective chapter II part E section 2.

²³⁸ Note that Burke-White, W. W. and von Standen, A., *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties* part V section B subsection 1 does not formally identify proportionality as the fourth standard of review alternative. Instead, it cites the European Court of Human Rights practice relating to the margin of appreciation concept as holding this position. This thesis however, as seen in section 3.1.4, considers the standard of review and the intensity of review to be independent, though interrelated, concepts. Furthermore, the standard of review of the ECHR Court has been deemed as proportionality (see section 3.2.3). Therefore, it considers that the fourth standard of review alternative to be found in international law practice is proportionality rather than the margin-of-appreciationish concept that Burke-White and von Standen refers to in their article.

Looking to arbitration practice for inspiration in resolving this issue, it is evident that measures depriving the investors of substantial monetary value not were considered disproportional in relation to the possibility of Argentinean financial breakdown in the *Continental Casualty* award.²³⁹ Xanadu might be facing substantial environmental problems in the event of continued unobtainium extraction, while the RDA stands at the brink of financial collapse if the ban on extraction continues. Relative to the *Continental Casualty* case, the investor interests in favour of disproportionality are thus perhaps somewhat more pronounced in the Xanadu case. At the same time, environmental issues have been proved to carry substantial weight in cases such as *Methanex v United States*.²⁴⁰ Since a continued unobtainium extraction would have severe effects on Xanadu's environment, it might therefore be assumed that the Xanaduian government's measures were proportional to the harm suffered by the RDA. Article 18 of the US-Xanadu BIT would thus exclude Xanadu from liability also under a review based on the proportionality standard.

The four standards of review now presented are, as seen, those usually relied upon when international tribunals need conduct a balancing of competing norms, interests and values. To complete the picture, however, a few remarks on the standards of review relied upon by US courts are merited: While most other countries of the western hemisphere have embraced proportionality as the applicable standard of review within their respective municipal law,²⁴¹ US courts currently utilize a range of standards relative to which kinds of norms interests and values that are to be balanced against one another.²⁴² This system is thus very much interlaced with the underlying structure of US jurisprudence, and in particular its constitutional law. As for the actual standards of review relied upon, the range

²³⁹ See *Continental Casualty* paragraphs 231-232.

²⁴⁰ See *Methanex v United States* part IV chapter E paragraph 20.

²⁴¹ See Sweet, A. S. and Mathews, J., *Proportionality Balancing and Global Constitutionalism* part IV section A page 113.

²⁴² See Sullivan, E. T. and Frase, R. S., *Proportionality Principles in American Law: Controlling Excessive Government Actions* chapter II part 3 page 53.

stretches from proportionality-like “strict scrutiny review”,²⁴³ through “intermediate scrutiny” which not is unlike least restrictive means analysis,²⁴⁴ to “rational basis testing” which resembles the suitability test of proportionality.²⁴⁵ Since both proportionality and least restrictive means analysis already have been discussed, the only really new standard of review alternative that US law thus might be said to present the Xanadu-tribunal with is rational basis testing.²⁴⁶ As it already have been shown that the ban on unobtainium extraction obviously is appropriate to achieve the objective pursued, Xanadu would evidently be excluded from liability by article 18 of the US-Xanadu BIT also under a review based on this standard.

5.1.3 So, which one is it?

Having sketched out the alternative standards of review the tribunal might employ in evaluating whether the NPM clause of article 18 of the BIT may exclude Xanadu from liability; the question now is which one it should utilize. As was indicated in section 5.1.1 above, the wording of the nexus requirement might here constitute something of a basis. The nexus of article 18 states that the measure in question must be “necessary for” the pursuit of the relevant aim. Article 31 of the Vienna Convention holds that ‘a treaty shall be interpreted [...] in accordance with the ordinary meaning to be given to the terms of the treaty in their context’. The wording of the nexus pulls the thoughts in the direction of least restrictive means analysis since this one emphasizes the necessity test, but that is not the

²⁴³ See *ibid.* chapter II part 3 section A.

²⁴⁴ See *ibid.* chapter II part 3 section B.

²⁴⁵ See *ibid.* chapter II part 3 section C.

²⁴⁶ Note that a standard of review known as rational basis with a bite also have been identified by some commentators, see for instance Sullivan, E. T. and Frase, R. S., *Proportionality Principles in American Law: Controlling Excessive Government Actions* chapter II part 3 section C subsection 2 and Pettinga, G. L., *Rational Basis With Bite: Intermediate Scrutiny by Any Other Name* in general. This standard would seem to involve a stricter suitability test, but does not otherwise stray too far from rational basis testing. It would furthermore appear to be a standard somewhat unique to US law, and it will therefore not be further discussed here.

end of the story.

The Vienna Convention article 31 namely also holds that a treaty shall be interpreted ‘in the light of its object and purpose’. The purpose of a BIT is first and foremost investment protection.²⁴⁷ Thus the interpretation of the nexus conveying the strongest protection to the RDA right of extraction might be given preference. Of the alternatives listed above, choice constrained validity clearly holds this position since it, as seen, more or less always would exempt preclusion of liability. Note furthermore that between least restrictive means analysis and proportionality, the latter necessarily will provide the stronger protection.²⁴⁸ However, presumptions about interpretations of NPM clauses based on objects and purposes ‘should be used with caution since they provide ready-made generalized rule[s] that may not fit in a particular case or be faithful to the intentions of treaty partners’²⁴⁹. Also, such presumptions may often be counteracted by other presumptions, for instance the proposition that treaty obligations, as derogations of sovereignty, should be subject to a restrictive interpretation.²⁵⁰ The weight of the presumption-argument in favour of choice constrained validity should for these reasons not be exaggerated.

Another interpretive factor to be taken into account is arbitration practice.²⁵¹ A common consensus relating to the applicable standard of review within an international investment law NPM clause context has yet to crystallize, however. As for the latest decision relating to an NPM clause of “necessary for”-terminology, *Continental Casualty*, it would seem to lean towards the proportionality standard.²⁵² That tribunal’s application of proportionality is not entirely clean though, as it includes in the necessity test a question of

²⁴⁷ See above as well as for instance *Enron v Argentina* paragraph 331.

²⁴⁸ See section 5.1.4 below.

²⁴⁹ Newcombe, A. and Paradell, L., *Law and Practice of Investment Treaties* chapter 10 part I § 10.3 page 485.

²⁵⁰ See *SGS v Pakistan* paragraph 171.

²⁵¹ See section 2.3.

²⁵² See *Continental Casualty* chapter VI part D, in particular section B and paragraph 227, as well as Sweet, A. S., *Investor-State Arbitration: Proportionality’s New Frontier* part IV page 43. The approach is criticized in Alvarez, J. E. and Brink, T., *Revisiting the Necessity Defence: Continental Casualty v Argentina* part III.

‘whether [Argentina] could have adopted at some earlier time different policies that would have avoided or prevented the situation that brought about the adoption of the measures challenged’²⁵³. The proportionality standard in comparison, as developed above in chapter 3, limits the necessity test to alternative measures that might have been available at the time the measure in question was initiated. In fact, to suggest that a state needs to dispose itself of a problem before it has ever occurred would seem a bit like a logical fallacy in terms of causality. Even so, the standard of review applied by the *Continental Casualty* tribunal definitely lies closer to proportionality than to any of the other alternatives outlined in section 5.1.2, regardless of whether it applied one of the tests therein in an odd manner. If the Xanadu tribunal was to place decisive weight on the persuasiveness of the most recent jurisprudence, proportionality would thus be the applicable alternative. Note that an annulment decision on the *Continental Casualty* case currently is pending.

Three earlier awards assume an entirely different position than does *Continental Casualty* by equating the standard of review under a BIT provision using “necessary for”-terminology with the standard of review under the customary necessity defence of article 25 of the Draft Articles on State Responsibility, and finding the latter to be the choice constrained validity.²⁵⁴ The awards are *CMS v Argentina*²⁵⁵, *Enron v Argentina*²⁵⁶ and *Sempra v Argentina*²⁵⁷. The *Sempra* award was subsequently annulled for this explicit reason.²⁵⁸ As for the *CMS* and *Enron* awards, both of these have also been annulled (only partly in *CMS*’ case), but on other grounds than wrong standard of review application under their BIT NPM clause evaluations. Nevertheless, the annulment committee did, in the *CMS v Argentina: Decision on Annulment*, severely criticize the *CMS* award for equating the

²⁵³ See *Continental Casualty* paragraph 198.

²⁵⁴ More on this in section 5.2.1.

²⁵⁵ See *CMS v Argentina* paragraphs 315-378. Note that this tribunal makes a show of discussing the NPM clauses of the Draft Articles and the BIT separately, but in substance the latter discussion draws heavily on the former. See Kurtz, J., *Adjudging the Exceptional at International Investment Law: Security, Public Order and Financial Crisis* part III section A page 341.

²⁵⁶ See *Enron v Argentina* paragraphs 288-342, in particular paragraphs 333-334.

²⁵⁷ See *Sempra v Argentina* paragraphs 364-391.

²⁵⁸ See *Sempra v Argentina: Decision on Annulment* paragraphs 199 and 208.

NPM clause of the BIT in question with article 25 of the Draft Articles.²⁵⁹ In the *Enron v Argentina: Decision on Annulment*, the annulment committee annulled the initial award on the ground that the standard of review utilized under the scrutiny of article 25 of the Draft Articles was tainted with error,²⁶⁰ but refused to consider whether the initial award had erred with respect to equating it with the nexus requirement of the NPM clause of the US-Argentina BIT.²⁶¹ In sum, the three awards, as a consequence of they subsequently being annulled, would seem to constitute a tendency against the prospect of utilizing choice constrained validity as the preferred standard of review, especially on the basis that article 18 of the BIT should be equated with article 25 of the Draft Articles.²⁶² The cited paragraphs of the *CMS* and *Sempra* annulment decisions would explicitly seem to affirm this assertion.

In addition to the *Continental Casualty*, *CMS*, *Enron* and *Sempra* decisions, one more award tackling an Argentine NPM clause defence presently exists: In *LG&E v Argentina*, the NPM clause in question was found to exempt Argentina from liability without the tribunal conducting very much of an explicit review of the nexus requirement at all.²⁶³ Some lip service was paid to it in noting that no other alternative means were available to Argentina,²⁶⁴ but it is impossible to say whether the tribunal utilized choice constrained validity, least restrictive means analysis or some entirely different standard of review to reach this result.²⁶⁵ The award is thus not very helpful to the Xanadu-tribunal in its analysis of which standard of review to apply. It is worth noting that an Appellate Body decision on the *LG&E* case currently is pending.

Having now outlined the principle starting points of interpretation, the aim is for the Xanadu-tribunal to dissect each of the four alternative standards of review indicated in

²⁵⁹ See *CMS v Argentina: Decision on Annulment* paragraphs 128-131.

²⁶⁰ See *Enron v Argentina: Decision on Annulment* paragraphs 355-395.

²⁶¹ See *ibid.* paragraphs 403-405.

²⁶² See section 5.3.

²⁶³ See *LG&E v Argentina* paragraphs 226-258.

²⁶⁴ See *ibid.* paragraph 257.

²⁶⁵ See Kurtz, J., *Adjudging the Exceptional at International Investment Law: Security, Public Order and Financial Crisis* part IV section C.

section 5.1.2 in turn, and thus, ideally, find which one currently commands the most prominent juridical support. The US standard of review approach will not be reviewed since it, as mentioned, is very much interlaced with the underlying structure of US jurisprudence, and therefore may be considered of limited applicability in juridical circumstances not based on US law.

Starting off, for structural reasons, with “self-defence-reliant necessity evaluation”, this interpretation alternative seems to fit poorly with the context, object and purpose of article 18 of the US-Xanadu BIT: While the scope of most international investment law NPM clauses is polyphased in covering a multitude of circumstances,²⁶⁶ the context in which the self-defence-reliant necessity evaluation so far has been utilized only concerns self defence in the narrow sense.²⁶⁷ This is not to say that this standard of review is fundamentally inapplicable within international investment law boundaries, but rather that both the interpretive factors emphasized by article 31 of the Vienna Convention and the arbitration practice cited above depreciate this alternative relative to the other options. It is thus unlikely that the Xanadu-tribunal would choose self-defence-reliant necessity evaluation as the standard of review to be utilized.

A somewhat more probable possibility is “choice constrained validity”. In WTO law, a much quoted citation of Appellate Body jurisprudence has been that ‘the term “necessary” refers, in our view, to a range of degrees of necessity. At one end of this continuum lies “necessary” understood as “indispensable”; at the other end, is “necessary” taken to mean as “making a contribution to”’²⁶⁸. Under such a terminology, the choice constrained validity standard would equate “necessary” with “indispensable”, and, as seen, transform the standard of review concept from a principle into a rule. Since, however, the actual wording of article 18 of the BIT is “necessary for” rather than “indispensable for”, an interpretation of the NPM clause favouring choice constrained validity would initially appear somewhat

²⁶⁶ According to its wording, article 9 of the US-Xanadu BIT, for instance, covers Xanadu’s responsibilities as to maintenance of public order, international peace and security, its own essential security interests and human, animal and plant life, and health.

²⁶⁷ See section 5.1.2 above.

²⁶⁸ *Korea – Various Measures on Beef* paragraph 161.

inconsistent when viewed in the light of article 31 first paragraph of the Vienna Convention which states that ‘a treaty shall be interpreted [...] in accordance with the ordinary meaning to be given to the terms of the treaty’: The ordinary meaning of “necessary for” is definitely not only “indispensable for”.

On the other hand, it may and have been argued that the NPM clauses of the US BIT program (of which it can be assumed that the US-Xanadu BIT is a part) were drafted with the intention of being but a cross-reference to the customary international law defence of necessity as codified by article 25 of the Draft Articles of State Responsibility.²⁶⁹ Since the intent of the parties is listed as an interpretive factor in the Vienna Convention article 31, this argument may favour equating the interpretation of “necessary for” in article 18 of the US-Xanadu BIT with the interpretation of the nexus requirement in article 25 of the Draft Articles. The latter, as shall be further explored in section 5.2.1, prescribes choice constrained validity as the applicable standard of review. Choice constrained validity has also been favoured by commentators emphasizing that all BIT articles should be interpreted in the direction of investment protection as the fundamental object and purpose of investment treaties.²⁷⁰ This standard of review is namely the alternative that offers the best investment protection in that it limits state preclusion the most.²⁷¹

Note, however, that equating article 18 of the US-Xanadu BIT with article 25 of the Draft Articles in principle is a different concept than interpreting the necessity terminology under both articles to accommodate the same standard of review. The initial argument of the preceding paragraph may thus, at best, be deemed circumstantial.²⁷² Furthermore, it has already been shown that ICSID tribunals actually are disinclined to equate the articles, a disposition further weakening the cited circumstantial evidence. As for the object-and-

²⁶⁹ See Alvarez, J. E. and Khamsi, K., *The Argentine Crisis and Foreign Investors: A Glimpse Into the Heart of the Investment Regime* part III section C subsection 1 pages 429-431. Note that the weight of the following argument obviously would diminish in the context of a BIT, MIT or investment contract not purportedly drafted to reflect the customary necessity defence.

²⁷⁰ Ibid. part III section C subsection 1 pages 433-434. See also section 5.1.1 above.

²⁷¹ See section 5.1.4.

²⁷² The claim of equation in itself will be further explored in section 5.3.

purpose-argument, it is limited by the factors already explored in section 5.1.1, especially by possible opposing interpretive principles and alternative purposes. While it is correct that the object and purpose of the BIT is investment protection, the object and purpose of the NPM clause in isolation is to provide Xanadu with leeway in exceptional circumstances. To read into it a standard which would essentially truncate it under almost all thinkable scenarios would thus seem to, though following the object and purpose of the BIT, go against the object and purpose of the NPM clause itself.

In sum, taking especially account of the wording of article 18 as well as the ICSID annulment decisions on the *Sempra*, *CMS* and *Enron* cases, settling on choice constrained validity as the applicable standard of review would seem an unlikely choice for the tribunal of the RDA-Xanadu arbitration. Do mind that only the issue of which standard of review to utilize under article 18 thereby has been somewhat delimited. The issue of equating, in general, article 18 with article 25 of the Draft Articles will be sought further illuminated in section 5.3 below.

The third possible standard of review is “least restrictive means analysis”. As mentioned, this alternative might be the one best in tune with the wording of article 18. On the other hand, this one is also the alternative most lenient on host state legislative latitude and thereby least in tune with investment protection as the object and purpose of the BIT.²⁷³ No arbitration tribunals have to date directly favoured least restrictive means analysis as the preferred NPM clause standard of review, but it has been cited as such in some WTO law jurisprudence.²⁷⁴ The latter is currently somewhat inconsistent at the aggregate level as to which standard of review that is to be preferred, though.²⁷⁵

This lack of indicative case law coupled with a somewhat ambivalent interpretive foundation equates into situation under which the merits of least restrictive means analysis

²⁷³ Choice constrained validity and self-defence-reliant necessity evaluation sets, as seen, more stringent necessity tests, while proportionality adds an additional hurdle to be transversed by the state in proving itself precluded from liability.

²⁷⁴ See for instance *European Community – Measures Affecting Asbestos* paragraphs 164-175, as well as Van den Bossche, P., *Looking for Proportionality in WTO Law* part 6 pages 290-292.

²⁷⁵ See section 3.2.3.

are difficult to assess. That investment tribunals so far have been unwilling to utilize its prospects, however, might in itself constitute an argument against its utility. Furthermore, though it might be partly offset by other factors, the object and purpose of the US-Xanadu BIT in terms of investment protection might disfavour least restrictive means analysis relative to the other, stricter, standard of review alternatives: As the standard most lenient on state sovereignty, least restrictive means analysis might appear less appealing to an ICSID tribunal concerned with taking more than a minimum of account of such object and purpose argumentation.²⁷⁶ Relying on indistinct and fragmentary practice from WTO law would appear as too weak a basis for the Xanadu-tribunal to adopt in order to offset these considerations, at least unless it decided to grant decisive weight to the wording of article 18. In sum, least restrictive means analysis is thus a possible, but perhaps slightly awkward standard of review alternative for the tribunal to choose.

The final interpretive possibility is “proportionality”. Again, the wording of article 18 of the US-Xanadu BIT does disfavour this one somewhat relative to least restrictive means analysis since “necessary for” would seem to highlight the necessity test alone: Unlike the least restrictive means analysis, the proportionality standard takes a step beyond necessity in adding a proportionality *stricto sensu* test. Relative to the choice constrained validity standard, however, proportionality would seem to be the one favoured by the wording of the BIT: While the former equates “necessary for” with “indispensable for” (thereby turning article 18 into a rule), the latter does not push the standard that far from its terminological basis. In terms of the continuum of the *Korea – Various Measures on Beef* WTO award, proportionality would thus situate the standard of review closer to the pole of indispensable than least restrictive means analysis, but not on the top of that pole as does choice constrained validity. It might therefore be viewed as sort of a middle ground standard in terms of wording.

As for object and purpose of the BIT, the proportionality standard takes more account of investment protection than least restrictive means analysis: While not as stringent as

²⁷⁶ A tribunal interested in uniting the interests of the opposing parties into a balanced and sensible award that ideally should be commonly accepted as the correct judgement given the premises of the case at hand might fall into this category.

choice constrained validity, it poses an additional test for any government measure to transverse before the state is precluded from liability on account of it. In that sense, it might appeal to a tribunal trying to conjure up an award which weights in the arguments of both parties to the dispute since it thus is situated on middle ground also in terms of strictness.²⁷⁷

The current case law situation would also seem to favour proportionality. As it turns out, one of the two only (presently) unannulled arbitration awards dealing with investment law NPM clauses is *Continental Casualty*,²⁷⁸ and this one would seem to rely on the proportionality standard.²⁷⁹ More specifically, paragraphs 196-197 deals with the suitability test, paragraphs 198-230 with the necessity test and paragraphs 231-233 with the proportionality *stricto sensu* test. As mentioned above, the analysis under the necessity test is a bit off in relation to the standard established in section 3.1.2, but this does not intrinsically cause the persuasiveness of the award in terms of endorsing the proportionality framework as such to waver too much: The tribunal still works its way through the cumulative steps in paragraphs 196-233, and still refers to its own analysis as proportionality in paragraph 227. It might at this point also be prudent to adduce that the tribunal, in paragraphs 234-236, would seem to denounce the standard of review utilized in evaluating article 25 of the Draft Articles (which is, as shall be seen below, choice constrained validity) as an applicable alternative.

In conclusion, the proportionality standard would thus seem to have a lot going for it in terms of being situated in between least restrictive means analysis and choice constrained validity both on a strictness scale relating to preclusion of liability, and in relation to wording: It takes somewhat more account of the investment protection argument than does the former at the same time as it is more in accordance with the wording of article 18 than the latter. Furthermore, it is supported by the present case law situation, this one albeit

²⁷⁷ See section 5.1.4 just below.

²⁷⁸ The other one is *LG&E v Argentina*. As has been shown, that award remains indecisive as to which standard of review it prefers utilized, however.

²⁷⁹ The *CMS* award is in principle also unannulled as to its decision on the NPM clause preclusion. However, the *CMS v Argentina: Decision on Annulment* did severely criticize its approach. Its value as a precedent based on its persuasiveness is for this reason limited.

somewhat on the slim side (most awards having been annulled). In total, the proportionality standard is not an unlikely choice for the US-Xanadu tribunal to end up preferring.

As for differently worded NPM clauses, a concrete evaluation will probably have to be undertaken in each distinct case. Had article 18 of the US-Xanadu BIT read “indispensable for” instead of “necessary for” for instance, the above argumentation relating to article 31 first alternative of the Vienna Convention would have favoured choice constrained validity, in turn possibly affecting the tribunal’s choice of standard of review approach. Other examples of differently worded NPM clauses include “directed to”²⁸⁰, “required to”²⁸¹, “for the reasons of”²⁸² and “in the interest of”²⁸³ just to name a few. The wording of the NPM clause in question is, as seen, but one factor among several taken into account when determining the proper standard of review, however. Its practical merits must therefore be balanced against the other factors highlighted by article 31 of the Vienna Convention in each distinct case of evaluation.

5.1.4 Proportionality’s potential

Though its potential not can be said to entirely tip the issue, the proportionality standard does, as explored in the second to last paragraph of section 5.1.3, perhaps possess a certain aptitude as a favoured instrument on which to hinge the nexus of an NPM clause balancing operation: If it is assumed that the alternatives presented in section 5.1.2 are exhaustive,²⁸⁴ proportionality would seem to be situated on middle ground along several

²⁸⁰ See the New Zealand-China Agreement on the Promotion and Protection of Investments article 11.

²⁸¹ See the Kazakhstan-Belgium-Luxemburg Agreement on the Reciprocal Promotion and Protection of Investments article 3 paragraph 3.

²⁸² See the Germany-Haiti Treaty Concerning the Promotion and Reciprocal Protection of Capital Investment article 2 alternative A.

²⁸³ See the Germany-Russia Agreement Concerning the Promotion and Reciprocal Protection of Investments article 2 alternative C.

²⁸⁴ This is obviously not the case in practice since, as has been shown, any multitude of imaginable standards of review could be constructed. However, the alternatives presented do appear to be the relevant options in terms of utility elsewhere in international law. To extend the range of alternatives beyond these options would

axes. Middle ground may, in turn, be the preferred field of operation for tribunals whose work entails equating strong opposing positions. Thus, the proportionality standard might appear appealing relative to the alternatives.

Relative to choice constrained validity on the one side, proportionality sets a less stringent standard in terms of precluding liability. While the former demands that no other alternatives present themselves under the necessity test, the latter states that precluding liability initially only requires a lack of less restrictive alternatives. Proportionality furthermore demands, though, that a proportionality *stricto sensu* analysis subsequently is conducted. In theory, a situation under which a measure that was deemed precluded by the choice constrained validity standard and, as a result, also by the necessity stage of the proportionality standard, is considered disproportional under the proportionality *stricto sensu* analysis is thus imaginable. In such a case, the proportionality standard would be the stricter alternative. In terms of the Xanadu arbitration, this would be the situation if it was found that Xanadu simply had no other options than banning unobtainium extraction, at the same time as the positive, environmental effects of that measure was deemed disproportional to the negative effects of making the RDA extraction rights virtually valueless. However, such a situation, where there simply exists no host state decision latitude at all, does appear more or less unimaginable.²⁸⁵ As long as that is the case, the relative difference of the strictness of the necessity tests dictates the relative strictness of the two standards of review as such, and choice-constrained validity does, as seen, sport the strictest test by equating “necessary for” with “indispensable for”.

If the nexus of article 18 of the US-Xanadu BIT was deemed to reflect the choice constrained validity standard, article 18 would therefore become more or less valueless as a NPM clause since its criteria almost never could get satisfied. Though such a thing definitely would strengthen investor rights, it would also face two opposing sentiments based on the object and purpose of the BIT: First, it would, as seen, go against the supposition that treaty obligations, as derogations of sovereignty, should be subject to a

thus seem to lead to a more theoretical discussion than the one conceptualized by this thesis.

²⁸⁵ If the costs (in the widest sense of the word) of the alternatives are disregarded, any situation will obviously present any actor with multiple possible courses of action.

restrictive interpretation.²⁸⁶ Second, it would confront the position that all treaty articles should be interpreted in a way that at least would give them a minuscule of effect.²⁸⁷ What would otherwise be the point of including them in the first place? This argument further connects with the presumption that the interpretation of treaties should be based on the intent(s) of the parties.²⁸⁸ Taking these assertions into account disfavors choice constrained validity as the preferred standard of review. Proportionality being the closest option to it in terms of strictness, it is the logical alternative for a tribunal placing emphasis on the object and purpose of the BIT in terms of investment protection to turn to next.

Relative to least restrictive means analysis on the other side, the proportionality standard adds an additional obstacle for the state measure to face in the form of the proportionality *stricto sensu* test. Given that the first two stages of proportionality analysis are wholly equated with the two stages under least restrictive means analysis,²⁸⁹ this would mean that proportionality is the stricter standard in terms of preclusion of liability, and therefore conveys tighter investment protection regulation.

In total, being less strict than choice constrained validity, but more than least restrictive means analysis, proportionality operates on middle ground in terms of strictness. As already seen, it is also a happy medium in terms of how literally close it is to the ordinary

²⁸⁶ See *SGS v Pakistan* paragraph 171.

²⁸⁷ See *Noble Ventures Inc. v Romania* paragraph 50, as well as Newcombe, A. and Paradell, L., *Law and Practice of Investment Treaties* chapter 2 part VII § 2.29 page 114.

²⁸⁸ See the Vienna Convention article 31 paragraph 4.

²⁸⁹ In light of the argumentation presented in sections 3.1.2 and 5.1.2, this would implicitly seem to be assumed. However, it is not unthinkable that different tribunals may utilize least restrictive means analysis and the first two stages of the proportionality analysis differently and thereby effectuate a discrepancy. Since there in international investment law yet have been no cases where the tribunal has resorted to least restrictive means analysis, a comparison hereunder is currently impossible. As for WTO law, it would seem that the standards of review utilized very much glide over in each other; from proportionality to some intermediate hybrid to least restrictive means analysis. See Kapterian, G., *A Critique of the WTO Jurisprudence on 'Necessity'* part 2 section C page 100. This would imply that, though not totally overlapping, least restrictive means analysis and the first two steps of proportionality analysis at least are considered quite close in terms of functionality.

meaning given to the “necessary for” wording (least restrictive means analysis being more in tune with it, while choice constrained validity being less so). Furthermore, proportionality incorporates an additional aspect into any balancing operation based on its framework than does the other alternatives (including self-defence-reliant necessity evaluation and rational basis testing for that matter): While they in principle only evaluate the measure in question against alternative measures, the proportionality standard, through its proportionality *stricto sensu* test, additionally equates it against the norms, interests and values asserted by the opposing party. Without striding too far into an intensity of review analysis, the crucial point to be noted is that it thereby may function as a steam valve against possibly adverse arbitrational results.

Imagine for instance the least restrictive alternative test being preferred by the Xanadu-tribunal, and that the ban on extraction thereby was considered necessary thus precluding Xanadu from liability. Imagine furthermore that this would obviously lead to RDA bankruptcy, at the same time as the positive effects on the Xanaduian environment actually would be minuscule in comparison. It may be argued that such a result would be inequitable and therefore defeat the fundamental purpose of balancing. If the tribunal had evaluated the NPM clause nexus under the proportionality standard on the other hand, it would have had the possibility to reject Xanadu’s argumentation on account of the relative disparity between the costs and the effects of the ban, and thus fashion an equitable award.

That such an option from time to time is valuable to possess is exemplified by WTO law practice. As seen, the Appellate Body has, in cases where it initially would appear to prefer least restrictive means analysis, tried to mix elements of the proportionality *stricto sensu* test into the necessity test.²⁹⁰ A much more lucid approach would have been to formally embrace proportionality as the optimal standard of review, based on the argument that this would further predictability and consistency within the relevant body of law.

In conclusion, proportionality’s potential lies both in its position as the middle ground standard of review alternative, and in its capacity to formally encompass a broader range of considerations than the other standards of review and thereby minimize the possibility of

²⁹⁰ See *Korea – Various Measures on Beef* paragraphs 164 onward and *US – Gambling* paragraphs 306-307 for instance.

unreasonable legal results.²⁹¹ Its potential might be considered concretized by its diffusion.²⁹² Note, though, that some commentators argue against this position by asserting that arbitration tribunals not are inherently equipped to conduct proportionality *stricto sensu* reviews at all,²⁹³ because such questions concern empirical and value-laden judgements best conducted by the state party as the authority on the local affairs of its nation.²⁹⁴ This should be properly identified as an issue of intensity of review rather than standard of review however, and is functionally therefore a separate topic from the one this thesis concerns itself with.²⁹⁵

5.2 The customary necessity defence

In a manner similar to the one it asserts under article 18 of the US-Xanadu BIT, Xanadu claims that the customary international law defence of necessity precludes it from any liability otherwise procured by the ban on unobtainium extraction. There would seem to be a general consensus among commentators and practitioners that this necessity defence is articulated by article 25 of the ILC Draft Articles on Responsibility of States for Internationally Wrongful Acts.²⁹⁶ As already stated, it is assumed that apart from the nexus

²⁹¹ See Kingsbury, B. and Schill, S., *Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law* part III pages 22-23.

²⁹² See section 3.2.

²⁹³ Kurtz, J., *Adjudging the Exceptional at International Investment Law: Security, Public Order and Financial Crisis* part V section B subsection 3 pages 367-368.

²⁹⁴ See Stein, E. (ed.) and Sandalow, T. (ed.), *Courts and Free Markets: Perspectives from the United States and Europe* chapter 1 pages 29-30.

²⁹⁵ See section 3.1.4 above. The terminology utilized in the assessment of this question is often concerned with whether or not the NPM clause in question is “self-judging”. Though it falls beyond the scope of this thesis to tackle the issue, it might be noted that no BIT NPM provision to date have been deemed (entirely) self-judging in nature. See Bjorklund, A. K., *Emergency Exceptions: State of Necessity and Force Majeure* part 5 section A, which provides a comprehensive review of the matter.

²⁹⁶ See Alvarez, J. E. and Brink, T., *Revisiting the Necessity Defence: Continental Casualty v Argentina* part 3 section A page 11 and Burke-White, W. W. and von Standen, A., *Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment*

requirement, Xanadu fulfils all the other criteria that article 25 sets. The question of preclusion thus (again) hinges on the nexus.

5.2.1 *The standard of review applicable*

The nexus of article 25 of the Draft Articles on State Responsibility has a quite different wording than did article 18 of the US-Xanadu BIT. While the latter states that the measure in question needs to be “necessary for” safeguarding the aim pursued, the former holds that the measure must be “the only way for the state to safeguard” that aim. This fairly strong articulation points, interpreted in the light of article 31 first paragraph of the Vienna Convention, towards a very strict standard of review in more or less explicitly stating the central tenet of the choice constrained validity standard. Such an interpretation is also supported by the ILC commentaries on the article,²⁹⁷ which may be viewed as preparatory work in accordance with article 32 of the Vienna Convention.

Taking into account case law within the international investment field, this picture recently turned slightly blurry though: While both the original *CMS*, *Enron* and *Sempra* awards would seem to endorse choice constrained validity as the preferred standard of review under article 25 of the Draft Articles,²⁹⁸ their annulment decisions not only dampen their impact, but also, in *Enron*’s case, seem to open for the possibility that other standards of review could be applicable to the nexus of article 25.²⁹⁹ As for the *Continental Casualty* and the *Vivendi II: Decision on Annulment* awards, neither directly discusses the issue, but it would appear that they both implicitly assume the article 25 nexus standard to be quite

Treaties part VII section A page 387, as well as Bjorklund, A. K., *Emergency Exceptions: State of Necessity and Force Majeure* part 2 page 474 and Rosenstock, R. and Kaplan, M., *The Fifty-third Session of the International Law Commission* section I. As for case law, see for instance *LG&E v Argentina* paragraph 245 and *Enron v Argentina: Decision on Annulment* paragraph 356 among others.

²⁹⁷ See International Law Commission, *Responsibility of States for Internationally Wrongful Acts* article 25 paragraph 15.

²⁹⁸ See *CMS v Argentina* paragraphs 323-324, *Enron v Argentina* paragraphs 304-313 and *Sempra v Argentina* paragraphs 350-351.

²⁹⁹ See *Enron v Argentina: Decision on Annulment* paragraphs 367-377.

strict.³⁰⁰

In other words: there is a fairly strong terminological and factual basis for concluding that the standard of review under article 25 of the Draft Articles is choice constrained validity. However, the recent annulment decision on the *Enron* case is causing some chaos since it would seem to annul the *Enron* award on the basis that it applied article 25 wrongly in not explicitly assessing whether choice-constrained validity actually was the correct standard of review to be utilized.³⁰¹ It furthermore seems open to the possibility that, despite its wording, article 25 should take into account reasonableness, thereby pushing the underlying standard of review away from choice constrained validity and towards least restrictive means analysis or something similar.³⁰² Note though, that the Annulment Committee limits itself to pointing out these possible adverse interpretations, and does not directly state that it favours one over the others.³⁰³ The antagonistic effect of the award should for that reason not be overstated.

Since the necessity defence of article 25 of the Draft Articles is based on customary international law, its content is not solely reliant on international investment law practice however. In fact, its customary character makes it subject to case law and authoritative argumentation from all fields of international law. To pinpoint the proper standard of review applicable, it is therefore necessary to broaden the horizon. Looking to ICJ practice, the *Gabcíkovo-Nagymaros Project* case would seem to be the operative decision.³⁰⁴ The court here applies a fairly strict standard to its nexus assessment,³⁰⁵ and it proceeds along

³⁰⁰ See *Continental Casualty v Argentina* part VI section A and paragraph 222, and *Compañía de Aguas del Aconquija v Argentina, Resubmitted Case: Decision on Annulment* paragraph 260.

³⁰¹ See *Enron v Argentina: Decision on Annulment* paragraphs 367-377 and 405.

³⁰² See *ibid.* paragraphs 370-371.

³⁰³ See *ibid.* paragraph 373.

³⁰⁴ See Hill, S. F., *The "Necessity Defence" and the Emerging Arbitral Conflict in its Application to the U.S.-Argentina Bilateral Investment Treaty* part IV page 554 and Agius, M., *The Invocation of Necessity in International Law* part 2 section 2.2 page 105.

³⁰⁵ See *Gabcíkovo-Nagymaros Project* paragraph 55. Note that this award was subject to the previous version of the Draft Articles under which the necessity defence was located in article 33. The former article 33 and the present article 25 are, however, virtually identical.

the same line in the *Construction of a Wall* case.³⁰⁶ In sum, the ICJ practice would thus seem to support choice constrained validity as the standard of review applicable to the nexus of the necessity defence articulated in article 25 of the Draft Articles.

For the Xanadu-tribunal to conclude that choice constrained validity not is the preferred standard of review alternative to be utilized in evaluating the nexus of the customary necessity defence would subsequently be problematic. The *Enron v Argentina: Decision on Annulment* opens for the possibility, but in the face of argumentation based on the terminology of article 25, preparatory work and several tribunal awards over multiple juridical fields, that decision's somewhat inconclusive statements probably mount too weak an opposition. As it has already been shown that there were alternatives available to Xanadu other than banning the extraction of unobtainium outright, the criteria of article 25 of the Draft Articles are not fulfilled and the country may therefore not rely on the customary necessity defence to preclude itself from liability.

5.2.2 Proportionality's potential

Proportionality would not seem to attain much of a potential as the preferred standard of review to be utilized in evaluating the nexus of article 25 of the Draft Articles of State Responsibility under the conditions sketched out above. Its only hope may hinge on the articulations of the *Enron* annulment decision. It is there stated that 'another possible interpretation [than choice constrained validity] would be that there must be no alternative measure that the State might have taken for safeguarding the essential interest in question that did not involve a similar or graver breach of international law. [...] Under this interpretation, the principle of necessity will only be precluded if there is an alternative that would not involve a breach of international law or which would involve a less grave breach of international law'³⁰⁷. In other words, any alternative measures must be reasonable relative to how much they infer on the State's international duties. Furthermore, the decision also questions 'whether the relative effectiveness of alternative measures is to be

³⁰⁶ See *Construction of a Wall* paragraph 140.

³⁰⁷ *Enron v Argentina: Decision on Annulment* paragraph 370.

taken into account’³⁰⁸. If so, it may be argued that “the only way” only refers to measures of similar relative effectiveness, in turn meaning that the standard of review has drifted away from the rule-based alternative of choice constrained validity and towards a more principle-based standard in terms of least restrictive means analysis or proportionality.

By in this way being detached from the pole of indispensability on the continuum of the *Korea – Various Measures on Beef* case, the nexus of article 25 would be made subject to the host of considerations indicated in section 5.1.4 since it thereby attains the more mellow properties of a juridical principle at the expense of the stringency of a rule. Both proportionality’s position as a middle ground standard and its potential as steam valve against adverse arbitrational results would thus favour its utility.³⁰⁹ Again though, it is worth stressing that the current legal setting does not appear ready to deduct the nexus of article 25 from choice constrained validity as its functional standard of review, in spite of the articulations of *Enron* annulment decision. Proportionality’s potential in this respect is therefore currently a fairly hypothetical quantity.

5.3 Some notes on conflation

A slight digression from the main topic of exploring the merits of proportionality within international investment law is at this point warranted. As has already been indicated, the original *CMS*, *Sempra* and *Enron* awards all equated the NPM clause of the US-Argentina BIT with the customary defence of necessity as articulated by article 25 of the Draft Articles on State Responsibility.³¹⁰ The latter two awards were subsequently annulled (and the Annulment Committee also severely criticized the approach of the *CMS* tribunal without actually annulling its decision on those merits), but the prospect they

³⁰⁸ Ibid. paragraph 371.

³⁰⁹ See section 5.1.4.

³¹⁰ See *CMS v Argentina* paragraphs 308 and 374 (constituting an implicit equalization according to *CMS v Argentina: Decision on Annulment* paragraphs 123-127), *Sempra v Argentina* paragraphs 377-388 and *Enron v Argentina* paragraphs 333-340. See in general Bjorklund, A. K., *Emergency Exceptions: State of Necessity and Force Majeure* part 3 pages 492-496.

fronted have been endorsed by some commentators.³¹¹ A few remarks on this issue are therefore merited since it may influence the potential utility of the proportionality standard indirectly by altering the operational premises it is subject to.

5.3.1 *The argument*

‘The debate is essentially over whether [the NPM clause in question] means to displace relevant customary international law or, in more formal terms, is meant to be *lex specialis*’³¹². It is argued that any NPM clause, according to the first paragraph of article 31 of the Vienna Convention, should be interpreted in light of its object and purpose, and that the object and purpose of the NPM clauses within the context of the US BIT program is (or was) to simply refer to the customary necessity defence of the Draft Articles.³¹³ Thereby, US BIT NPM clauses, such as article 18 of the US-Xanadu BIT, do not constitute *lex specialis* provisions.³¹⁴

Furthermore, the argument goes that in accordance with the Vienna Convention article 31 third paragraph alternative C, the interpretation of an NPM clause needs to take into account any relevant rule of international law. The customary necessity defence being close in terms of functionality to article 18 of the BIT, a tribunal interpreting the latter must therefore necessarily include the former in its assessment. ‘Moreover, the defence of

³¹¹ See for instance Alvarez, J. E. and Khamsi, K., *The Argentine Crisis and Foreign Investors: A Glimpse Into the Heart of the Investment Regime* part III section C subsection 1 and Alvarez, J. E. and Brink, T., *Revisiting the Necessity Defence: Continental Casualty v Argentina* part III section B.

³¹² Ibid. part III section C page 427. Note that Kurtz, J., *Adjudging the Exceptional at International Investment Law: Security, Public Order and Financial Crisis* establish a somewhat more refined, triangular approach in parts III-V.

³¹³ See *ibid.* part III section C subsection 1 page 429-431.

³¹⁴ It should perhaps be noted that commentators arguing for conflating the NPM clauses of BITs with the customary necessity defence articulated in article 25 of the Draft Articles specifically discuss the Argentine case complex. Article 18 of the US-Xanadu BIT is not in total conformity with article IX of the US-Argentina BIT, and it might therefore be that those commentators would view the former differently. For the sake of argument however, it shall within this section of the thesis be assumed that the two NPM provisions may functionally be equated.

necessity is surely one of those fundamental rules of international law, such as exhaustion of local remedies, that requires very specific evidence of derogation³¹⁵. Also, the object and purpose of the BIT in terms of investment protection is in this respect being flaunted.³¹⁶ Finally, analogies are drawn from the ICJ *Oil Platforms* case, in which it was articulated that ‘the application of the relevant rules of international law relating to this question [of preclusion of liability] thus forms an integral part of the task of interpretation [of the relevant treaty NPM clause]’³¹⁷.

In total, though their actual assertions necessarily are a bit more sophisticated than the brief outline now traced, the commentators endorsing conflation would generally seem to agree with the *CMS*, *Sempra* and *Enron* tribunals in holding that the US-Argentina BIT NPM clause was not intended to and did not ‘deal with the legal elements necessary for the legitimate invocation of a state of necessity’³¹⁸. A discussion on the (lack of) self-judging character of BIT NPM provisions is also incorporated into this argumentation, thereby mixing the question of standard of review with a question of intensity of review.³¹⁹ In sum, the postulate appears to be that article IX of the US-Argentina BIT functioned simply as a placeholder for, and reference to, the necessity defence of customary law. In other words, ‘the *CMS*, *Enron* and *Sempra* tribunals interpreted the “only means” requirement under article 25 [of the Draft Articles] as fatal to the necessity plea under article XI [of the BIT], if any other means were available to Argentina’³²⁰. Such an understanding is positively based on the alleged intentions of the US BIT program, and negatively based on a truncation of any evidence to the opposite effect (for instance terminological asymmetry).

³¹⁵ Alvarez, J. E. and Khamisi, K., *The Argentine Crisis and Foreign Investors: A Glimpse Into the Heart of the Investment Regime* part III section C subsection 1 page 433 with a reference to the *Loewen Group Inc. v United States* case.

³¹⁶ See *ibid.* part III section C subsection 1 pages 433-434, as well as the discussion on the object and purpose of article 18 of the US-Xanadu BIT in section 5.1.3 above.

³¹⁷ *Oil Platforms* paragraph 41.

³¹⁸ *Sempra v Argentina* paragraph 378.

³¹⁹ See *CMS v Argentina* paragraphs 366-373, *Sempra v Argentina* paragraphs 379-385 and *Enron v Argentina* paragraphs 335-337. Also see section 3.1.4 above.

³²⁰ Sweet, A. S., *Investor-State Arbitration: Proportionality’s New Frontier* part IV page 72.

5.3.2 Critique and recent practice

Starting off with the wording of the NPM provisions under scrutiny relative to the wording of article 25 of the Draft Articles, a natural conflation would not seem to be the most obvious of interpretative possibilities: Not only does article 25 operate in the opposite polarity of the BIT NPM provisions,³²¹ but it also articulates the nexus differently. While the former holds that the measure in question must be “the only way to safeguard” the objective pursued, the latter only requires it to be “necessary for” safeguarding that aim. As was indicated in sections 5.1 and 5.2, this difference in wording favours different standards of review as the applicable one. The terminological asymmetry between the customary necessity defence and the BIT provisions thus constitutes an argument against conflation.

Looking secondly to the object and purpose of the BIT NPM provisions; the supporters of conflation seem to rely heavily on the assertion that (despite its wording) the drafters of the US-Argentina BIT intended article IX simply to refer to the customary necessity defence.³²² This argument is further supported by way of allusion to the alleged object and purpose of any BIT in providing investment protection.³²³ That these assertions carry some weight is indisputable. However, some additional details need to be acknowledged before any definite conclusions as to their aptitude may be drawn: First, it has already been shown that there are BIT objects and purposes which, if not totally negate the investment protection argument, at least moderate its character.³²⁴ Second, it does seem slightly odd

³²¹ Where the Draft Articles on State Responsibility article 25 states that ‘necessity may not be invoked by a State as a ground for precluding wrongfulness of an act not in conformity with an international obligation of that State unless the act [...] is the only way to ...’, article IX of the US-Argentina BIT (and article 18 of the US-Xanadu BIT for that matter) instead asserts that ‘this treaty shall not preclude the application by either party of measures necessary for ...’. Thus, while the former (directly) regulates the instances where necessity not may be invoked, the latter (directly) regulates the instances where it may. This terminological asymmetry does perhaps not equate into any practical fallout, but it does at least not promote an interpretation endorsing conflation.

³²² See Alvarez, J. E. and Khamsi, K., *The Argentine Crisis and Foreign Investors: A Glimpse Into the Heart of the Investment Regime* part III section C subsection 1 pages 429-431.

³²³ See *ibid.* pages 433-434.

³²⁴ See section 5.1.3.

that the BIT drafters not only found it prudent to include an unnecessary provision in the sense that it's content but referred to a rule of customary law, but also that they included the clause despite that it would obviously be truncated under more or less any thinkable scenario since it was to be subject to the choice constrained validity standard of review.³²⁵ Third, while it may be true that the purpose of the US with respect to article IX of the US-Argentina BIT (and in extension article 18 of the US-Xanadu BIT) was conflation,³²⁶ Argentina (and Xanadu) may have been differently disposed. Indeed, the only evidence to the contrary advances by commentators endorsing conflation is that Argentina was aware of the history behind the US BIT program.³²⁷ However, some level of awareness of the historical trends of US BITs does not necessarily equate into an intention of conformity with those trends, especially in light of the above-mentioned truncational consequence. In sum, though there might be said to exist a certain argumentative basis relating to an interpretation based on their object and purpose for equating US BIT NPM clauses with the customary necessity defence, it is doubtfully totally peremptory.

Turning thirdly to case law, recent developments would seem to further weaken the argument for conflation. Where previously both the *CMS*, *Sempra* and *Enron* awards seemed to endorse its prospects, their subsequent annulment decisions not only negate their impact, but would even appear to reverse the tide. The *CMS v Argentina: Decision on Annulment* and the *Enron v Argentina: Decision on Annulment* does notably not annul the principal awards on the basis of conflation, however. The latter does in fact refuse to consider the problem at all,³²⁸ and rather annuls on another basis.³²⁹ The *CMS* annulment committee also refuses to annul on the basis of conflation,³³⁰ but does discuss matter. In

³²⁵ See Bjorklund, A. K., *Emergency Exceptions: State of Necessity and Force Majeure* part 2 section B subsection iii page 485 as well as section 5.2.1 above.

³²⁶ See Alvarez, J. E. and Khamsi, K., *The Argentine Crisis and Foreign Investors: A Glimpse Into the Heart of the Investment Regime* part III section C subsection 1 pages 428-429 and part III section A.

³²⁷ See *ibid.* part III section C subsection 1 pages 428-429. It is suggested that any NPM clause within the BIT program was specifically intended only to refer to the customary necessity defence.

³²⁸ See *Enron v Argentina: Decision on Annulment* paragraph 403.

³²⁹ See *ibid.* paragraph 405.

³³⁰ See *CMS v Argentina: Decision on Annulment* paragraph s 135-136.

stating that ‘[the article XI of the US-Argentina BIT and article 25 of the Draft Articles on State Responsibility] have a different operation and content’³³¹, that ‘the excuse based on customary international law [can] only be subsidiary to the exclusion based on article XI’³³² and that ‘article XI and article 25 [...] cover the same field and the tribunal should have applied article XI as the *lex specialis* governing the matter and not article 25’³³³, the committee definitely made a case against conflation, albeit *in dicta*.

As for the *Sempra v Argentina: Decision on Annulment* award, this one annuls on the grounds of conflation.³³⁴ In its own words: ‘it is apparent from this comparison [between article XI of the BIT and article 25 of the Draft Articles] that article 25 does not offer a guide to *interpretation* of the terms used in article XI. The most that can be said is that certain words or expressions are the same or similar’³³⁵. Furthermore, ‘article 25 and article XI [...] deal with quite different situations’³³⁶. Through its fairly detailed analysis of the matter from paragraph 197 to paragraph 208, the committee would in general seem to refuse that there are any grounds for conflating the two articles at all.

To complete the tour of recent practice it should perhaps finally be noted that the *Vivendi II: Decision on Annulment* award not remarks upon the matter of conflation, even though it does concern itself with a defence of necessity. Instead it states that ‘both [parties] agree that the current state of the law on the defence of necessity is reflected in article 25 of the International Law Commission’s (ILC) Articles on the Responsibility of States for Internationally Wrongful Acts’³³⁷. It would thus appear that Argentina for some reason chose to base its case on the customary necessity defence alone in *Vivendi II*, disregarding the possibility of the US-Argentina BIT NPM clause. Thereby, scant guidance as to the relationship between the necessity defence of the Draft Articles and the defence

³³¹ Ibid. paragraph 131.

³³² Ibid. paragraph 132.

³³³ Ibid. paragraph 133.

³³⁴ See *Sempra v Argentina: Decision on Annulment* paragraphs 208, 219 and 223.

³³⁵ Ibid. paragraph 199.

³³⁶ Ibid. paragraph 200.

³³⁷ *Compañía de Aguas del Aconquija v Argentina, Resubmitted Case: Decision on Annulment* paragraph 251.

based on a BIT NPM provision may be inferred from this award.

In conclusion, recent annulment practice, together with the asymmetry in wording would seem to block any conflation of BIT NPM clauses and the customary defence of necessity as articulated by article 25 of the Draft Articles. Though it may be that the object and purpose of BITs under the US BIT program to a certain extent support such equation, especially the assertions of the *Sempra* annulment decision are too unequivocal to overlook. Thereby, the Xanadu-tribunal may be considered banned from conflating article 18 of the US-Xanadu BIT with the customary necessity rule of article 25 of the Draft Articles.

5.4 The fair and equitable treatment standard

The RDA claims that Xanadu is liable to pay compensation since it breached the fair and equitable treatment standard laid down in article 5 of the US-Xanadu BIT by banning all unobtainium extraction. Xanadu contests the assertion on the grounds that the mentioned standard should be interpreted in the context of the situation, and thus not may be considered breached. The tribunal must thus determine whether Xanadu awarded the RDA fair and equitable treatment. If the latter is deemed relative to any Xanaduian norms, interests and values, it will be faced with a balancing situation that in turn might beget proportionality.

5.4.1 A balancing standard

The fair and equitable treatment standard is a fairly flexible concept insulating the investor and his investment against adverse state behaviour.³³⁸ It is essentially intended to fill gaps that may be left by more specific standards of investment protection.³³⁹ A lot of ink has been spent on trying to clarify the concept's relation to international customary

³³⁸ See Reinisch, A., *Standards of Investment Protection* chapter 6 section A page 111.

³³⁹ See Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter VII part 1 section C.

law,³⁴⁰ pin down its content and to map out its borderlines and topography. The intent of this section is not to explore and embellish on such theory, but rather to inspect the merits of proportionality within the context of the fair and equitable treatment standard. A few initial, theoretical remarks on the standard are warranted to properly identify the scope of this discussion, but a reader seeking a comprehensive review of the concept should look elsewhere.³⁴¹ The main question sought answered here is instead whether the concept of fair and equitable treatment essentially involves balancing.

Fair and equitable treatment is basically a fairly vague term.³⁴² Its wording indicates that Xanadu is bound to treat the RDA and its investment at, or better than at, a certain threshold treatment level along a range of axes including vigilance and protection, due process and non-denial of justice, lack of arbitrariness and non-discrimination, and transparency and stability (hereunder respecting the investor's reasonable expectations).³⁴³ The discussion thereby usually turns towards the tangible content of the standard by way of case law and theoretical constructions. However, detailed knowledge of what constitutes fair and equitable treatment in the abstract is not required to evaluate proportionality's potential relative to the tribunal's process of assessment of whether the fair and equitable treatment standard was breached. The crucial question instead to focus upon is whether the

³⁴⁰ See OECD Directorate for Financial and Enterprise Affairs, *Fair and Equitable Treatment Standard in International Investment Law* part II

³⁴¹ Examples of in-depth analysis include Tudor, I., *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment* and Ortino, F. (ed.), Liberti, L. (ed.), Sheppard, A. (ed.) and Warner, H. (ed.), *Investment Treaty Law: Current Issues II* part II.

³⁴² This point is summed up nicely by Muchlinski, P., *Multinational Enterprises and the Law* part III chapter 17 section 2.3 page 625 in stating that 'the concept of fair and equitable treatment is not precisely defined. It offers a general point of departure in formulating an argument that the foreign investor has not been well treated by reason of discriminatory or other unfair measures being taken against its interests. It is, therefore, a concept that depends on the interpretation of specific facts for its content'. More or less the same thing has been put forward by arbitration tribunals, for instance in *Mondev v United States* paragraph 118 and *Waste Management v Mexico* paragraph 99. See also Kingsbury, B. and Schill, S., *Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law* part II (in particular section 8).

³⁴³ See Reinisch, A., *Standards of Investment Protection* chapter 6 section C.

environmental interests of Xanadu may be taken into account in the assessment.

If the fair and equitable treatment standard is considered relative to such norms, interests and values of the host state, a tribunal reviewing the standard will in practice find itself confronted with a balancing situation: On the one side stands the (possibly) adverse treatment of the investor; while on the other stands the state's (possibly) justified motivation for treating the investor that way. Proportionality may enter the equation here as the method utilized in the process of equating the opposing positions.

There are mixed views as to whether a breach of the fair and equitable treatment standard should be considered relative to opposing norms, interests and values, however. While some commentators endorse the sentiment,³⁴⁴ others hold that such entities only should be taken into account in the determination of compensation after a breach of the standard has been established.³⁴⁵ The latter opinion would necessarily preclude any utilization of proportionality since the opposing interests thus would be directly collated on the basis of a strictly quantitative appraisal. Any method employed for such an operation inevitably collapses into a simple mathematical summation.³⁴⁶ Investment practice, however, seem to favour the balancing approach: In *Saluka v Czech Republic*, the tribunal states this clearly in articulating that 'the determination of a breach of [the fair and equitable treatment standard] by the Czech Republic [...] requires a weighting of the claimant's legitimate and reasonable expectations on the one hand and the respondent's legitimate regulatory interests on the other'.³⁴⁷ That position would also seem to have been taken (albeit somewhat more indirectly) in the *S.D. Myers v Canada*³⁴⁸, *Parkerings-Compagniet v Lithuania*³⁴⁹, *Pope & Talbot v Canada*³⁵⁰ and *Enron v Argentina*³⁵¹ awards

³⁴⁴ See for instance Reinisch, A., *Standards of Investment Protection* chapter 6 section C pages 126-129 and Sweet, A. S., *Investor-State Arbitration: Proportionality's New Frontier* part III section B page 62.

³⁴⁵ See for instance Tudor, I., *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment* chapter 7 section 7.1.

³⁴⁶ One not-so-simple problem the tribunal thereby would face, though, is the valuation of the opposing (often qualitative) interests. An assessment of this issue falls beyond the scope of this thesis.

³⁴⁷ *Saluka v Czech Republic* paragraph 306.

³⁴⁸ See *S.D. Myers v Canada: First Partial Award* paragraph 263.

³⁴⁹ See *Parkerings-Compagniet v Lithuania* paragraphs 332-333.

among others. The most conspicuous conclusion would thus be to assume that the fair and equitable treatment standard includes a certain amount of balancing of the competing interests involved.³⁵²

5.4.2 *Proportionality's potential*

Concluding that the fair and equitable treatment standard incorporates balancing, one of the first questions the Xanadu-tribunal will face when reviewing the RDA's allegation of a breach of this standard is thus how it should go about in undertaking the required balancing operation. Again, since the standard is contained in a treaty, the tribunal might look to article 31 of the Vienna Convention for inspiration. As developed above, fair and equitable treatment is a fairly vague concept, whereby both the ordinary meaning of the term and its object and purpose convey little guidance.³⁵³ In tune with the argumentation of section 2.3, however, case law may also be taken into account based on its persuasiveness. The Xanadu-tribunal is therefore prone to turn to earlier international investment law arbitration awards for advice.

Starting off with the *Saluka* award since this one contained the most obvious endorsement of balancing; its lengthy assessment of whether the Czech Republic had breached the fair and equitable treatment standard does not contain any explicit utilization of proportionality.³⁵⁴ It may be that the tribunal took the norms, interests and values of the

³⁵⁰ See *Pope & Talbot v Canada: Award on Merits* paragraphs 123-128 and 155.

³⁵¹ See *Enron v Argentina* paragraph 261. Note that the annulment committee reviewing the *Enron* award endorses the *Enron* tribunal's assessment of the fair and equitable treatment standard, see *Enron v Argentina: Decision on Annulment* paragraphs 298-316.

³⁵² See Dolzer, R. and Schreuer, C., *Principles of International Investment Law* chapter VII part 1 section I and 129 and Sweet, A. S., *Investor-State Arbitration: Proportionality's New Frontier* part III section B as well as Kingsbury, B. and Schill, S., *Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law* part III section 3 subsection B.

³⁵³ See for instance Newcombe, A. and Paradell, L., *Law and Practice of Investment Treaties* chapter 6 part III § 6.19 page 263.

³⁵⁴ See *Saluka v Czech Republic* paragraphs 285-456.

state into account when reviewing the latter's conduct,³⁵⁵ but it did not formally do so by way of proportionality's methodological framework. Similar behaviour is apparent in the other cited awards as well.³⁵⁶ The trend seems instead to be that emphasis is placed on the state's conduct relative to the investors' expectations, with the state's interests but applied as a backdrop.³⁵⁷ This would seem to contrast the more active approach of proportionality which emphasizes not only the relation between the state's and the investor's interests (through the proportionality *stricto sensu* test), but also the state's duty to choose the least excessive of any reasonably available alternative measures (through the necessity test). Thus, if the Xanadu-tribunal was to follow the case law trend when evaluating Xanadu's possible breach of the fair and equitable treatment standard of article 5 of the US-Xanadu BIT, it would rather approach the balancing process indirectly through a reasonable expectations assessment than utilize the proportionality standard to equate the opposing positions directly.

Does this mean that proportionality's potential is negligible in the context of the fair and equitable treatment standard? *De lege lata*, that would currently seem to be the case, but the postulate have earned some critical remarks *de lege ferenda*: On the one hand, proportionality, through its three-step framework, functionally comprises a fairly comprehensive method under which more than but a collation of the opposing legal positions is undertaken.³⁵⁸ The necessity test may, in other words, be considered to functionally stretch beyond the scope of the fair and equitable treatment standard which in essence limits its balancing component to but a weighting of the competing interests involved.³⁵⁹ If so, the proportionality principle should probably be excluded as a standard of review alternative for balancing in this context because it inherently incorporates

³⁵⁵ See for instance *ibid.* paragraphs 336-337.

³⁵⁶ See *S.D. Myers v Canada* paragraphs 258-269, *Parkerings-Compagniet v Lithuania* paragraphs 326-346 and *Enron v Argentina* paragraphs 256-268.

³⁵⁷ See Newcombe, A. and Paradell, L., *Law and Practice of Investment Treaties* chapter 6 part III § 6.26 page 282.

³⁵⁸ See section 3.1.

³⁵⁹ As an example of an award where this approach was applied, see *Saluka v Czech Republic* paragraph 306.

elements that the operative legal concept under review does not accommodate.

On the other hand, proportionality does, as seen, provide a fairly comprehensive methodological framework that promotes juridical predictability and consistency.³⁶⁰ It may thereby be argued that ‘although the [fair and equitable treatment standard] enhances arbitral flexibility, its very elasticity raises anxieties about (a) the scope of arbitral authority [...], and (b) the determinacy of rulings [...]. If one accepts that these worries are well-founded, then one can also see why the adoption of proportionality would make sense, in so far as it would inject a measure of analytic, or procedural, determinacy to the balancing exercise. Moreover, proportionality, properly used, requires arbitrators to reduce the losses accruing to the loser as much as is legally possible, thus enhancing their legitimacy’^{361 362}. The Xanadu-tribunal may find the rationale of this argument convincing enough to break with the consistency of international investment law arbitration practice and instead base its review of the fair and equitable treatment standard of article 5 of the US-Xanadu BIT on the proportionality standard.

5.5 Proportionality in other contexts

This section is intended as a short discussion on the utilization and diffusion of proportionality throughout the parts of international investment law not already discussed. Short it is since proportionality, as shall be seen, not has been utilized very much at all in such contexts.

5.5.1 *In theory*

Proportionality is a framework utilizable for equating two or more differing legal positions. It represents a three-step analytical tool that an international investment law

³⁶⁰ See Sweet, A. S. and Mathews, J., *Proportionality Balancing and Global Constitutionalism* part II section D subsection 3.

³⁶¹ Sweet, A. S., *Investor-State Arbitration: Proportionality's New Frontier* part III section B page 63.

³⁶² See section 3.1 above.

arbitration tribunal may employ when faced with a situation under which it is forced to balance any opposing legal norms, interests and values. Thus, proportionality is, in theory, a concept of general procedural applicability: Whenever a juridical predicament whose solution depends on balancing presents itself, the arbitration tribunal faced with it may resort to the proportionality framework.

To illustrate this point, a couple of examples are merited. Returning to the RDA-Xanadu case, its factual basis may be expanded to accommodate a range of balancing situations. For instance, assuming that the BIT between the US and Xanadu contained a non-disclosure provision relating to state secrets on Xanadu's side and confidential business information on the investor's (RDA's) side, that provision might be limited only to use of said information clearly contrary to some essential interests of the parties. Any subsequent award relating to it would thereby necessarily have to incorporate a balancing of those interests against the rights of non-disclosure protected by the provision. Similarly, if the BIT included any article allocating a duty to the RDA or Xanadu, but with the qualification that compliance with it not constitutes an unreasonable responsibility relative to the interests of the duty bound party, a tribunal assessing whether conduct contrary to the duty constitutes a breach of the BIT will face a juridical situation under which it must balance the interests protected by the duty with the interests protected by the qualification of reasonableness. Both these balancing situations could be resolved by way of the proportionality standard of review.

5.5.2 *In practice*

Besides the instances already accounted for, proportionality has only been utilized once in international investment law arbitration practice. That invocation occurred in 2003 in the *Tecmed v Mexico* ICSID arbitration. Mexican authorities did not renew a temporary operating license for a waste landfill held by a subsidiary of Tecmed, a Spanish company. Tecmed claimed that this omission, given the circumstances of the case, constituted an indirect (*de facto*) expropriation that was compensable under article 5 of the BIT between Spain and Mexico (the Spain-Mexico Agreement on the Reciprocal Promotion and

Protection of Investments) as the equivalent of expropriation.³⁶³ The tribunal held that ‘it is generally understood that [indirect expropriation] materializes through actions or conduct, which do not explicitly express the purpose of depriving one rights or assets, but actually have that effect’³⁶⁴. It furthermore stated that the expropriatory character of state actions was relative to the balance between the public interests presumably protected thereby and the protection granted to investors. ‘Although the analysis starts at the due deference owing to the State when defining the issues that affect its public policy or the interests of society as a whole, as well as the actions that will be implemented to protect such values, such situation does not prevent the Arbitral Tribunal, without thereby questioning such due deference, from examining the actions of the State in light of Article 5(1) of the Agreement to determine whether such measures are reasonable with respect to their goals, the deprivation of economic rights and the legitimate expectations of who suffered such deprivation. There must be a reasonable relationship of proportionality between the charge or weight imposed to the foreign investor and the aim sought to be realized by any expropriatory measure’³⁶⁵. The tribunal then went on to conduct a detailed proportionality *stricto sensu* analysis, and finally found that Mexico’s conduct had to be considered expropriatory.³⁶⁶

The *Tecmed v Mexico* award thereby placed all emphasis on the final stage of the three-step proportionality framework. Some notes on the necessity test may be found entwined in the proportionality *stricto sensu* assessment,³⁶⁷ but the tribunal’s approach cannot be said to strictly adhere to the proportionality formula outlined in section 3.1. However, relative to the alternative standards of review presented in section 5.1.2, the method utilized in *Tecmed v Mexico* must be said to favour proportionality as the preferred standard of review for balancing situations similar to the one there assessed. Indeed, in highlighting the proportionality *stricto sensu* analysis as much as it does, the award more or

³⁶³ See *Tecmed v Mexico* paragraphs 35-51.

³⁶⁴ *Ibid.* paragraph 114.

³⁶⁵ *Ibid.* paragraph 122.

³⁶⁶ See *ibid.* paragraphs 123-151.

³⁶⁷ See for instance *ibid.* paragraph 136.

less excludes any other standard of review than proportionality since none but that one incorporates proportionality *stricto sensu* test. It may definitely be criticized for jumbling the necessity and proportionality *stricto sensu* stages, thereby deterring juridical consistency and predictability,³⁶⁸ but it still must be considered an argument for the proportionality standard within international investment law per se.³⁶⁹

In conclusion, when determining whether a state measure may be considered indirectly expropriatory, the *Tecmed v Mexico* award not only purports that a balancing of competing interests is called for,³⁷⁰ but also pushes the assessing tribunal in the direction of proportionality. It would appear that this sentiment is implicitly endorsed by the *LG&E v Argentina* award.³⁷¹ From it all may be inferred that though proportionality not yet has attained total diffusion throughout international investment law, it does seem somewhat established as the preferred balancing method within some important sectors.

³⁶⁸ As seen in section 3.2.3, WTO jurisprudence is also the target of similar critique.

³⁶⁹ See Kingsbury, B. and Schill, S., *Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law* part III section 3 subsection A pages 34-35 and Sweet, A. S., *Investor-State Arbitration: Proportionality's New Frontier* part III section B page 64.

³⁷⁰ In this context, such a position is often termed the police power doctrine. See for instance Brunetti, M., *Indirect Expropriation in International Law* and Newcombe, A. and Paradell, L., *Law and Practice of Investment Treaties* chapter 7 part I § 7.25.

³⁷¹ See *LG&E v Argentina* paragraph 195.

6 Concluding remarks

This, final, chapter is intended to draw together all of the above argumentation in articulating a few concluding remarks on the issue of the present state and potential of proportionality in international investment law. Section 6.1 will try to enunciate a conclusion as to the extent of proportionality's present actual impact, while section 6.2 will advance some final opinions as to the utility of proportionality in terms of usability and practical prospects. Both sections assume familiarity with the discussions, references and conclusions articulated above as they are not intended develop new arguments, but rather consolidate the ones already advanced.

6.1 So, are we there yet?

In short; not quite, but there definitely are trends presently pulling international investment law towards a greater reliance on proportionality. Within NPM clause evaluation for instance, perhaps one of the most tangible areas of balancing in international investment law at the moment, the current configuration of interpretative factors would seem to favour proportionality.³⁷² The *Continental Casualty* award relies heavily on that standard of review in its assessment of whether Argentina might be precluded from liability, and as the most recent and, so-far, only unannulled decision of consequence relating to this question, it might, as seen, be argued to articulate the present operative juridical status regarding NPM clause evaluation in an international investment law context. An annulment decision on *Continental Casualty* is pending though, whereupon the ICSID Annulment Committee has the potential to either topple the budding trend or, perhaps preferably,³⁷³ add credence to its premise by firmly endorsing its utilization of proportionality as the preferred standard of review.

³⁷² See sections 5.1.3 and 5.1.4.

³⁷³ See section 6.2 just below.

Proportionality also seems to hold some ground within the context of balancing under an assessment relating to alleged indirect expropriation: The tribunal of *Tecmed v Mexico* relied heavily on a proportionality *stricto sensu* analysis in its appraisal of whether Mexico was liable for compensation, and the only formal standard of review that incorporates the proportionality *stricto sensu* test is proportionality. Thus, subsequent tribunals may be inclined to utilize the proportionality framework if they are to follow up on the path set out on by the *Tecmed* award. However, *Tecmed v Mexico* is starting to age a bit without any new awards directly adopting its argumentation having been released. International investment law meanwhile has developed at a rapid pace, whereupon the relative persuasiveness of the award might be starting to diminish. On the other hand, no new arguments against the utilization of proportionality within this context have subsequently surfaced, and proportionality also does possess a certain general utility.

In relation to fair and equitable treatment evaluations and the necessity defence based on article 25 of the Draft Articles of State Responsibility, proportionality does presently not seem to be the favoured method of assessment. While tribunals evaluating the former, though not directly dismissive of proportionality, seem to apply a slightly different balancing approach altogether, tribunals appraising the latter definitely utilize another standard of review alternative specifically. It should hereunder be noted, though, that article 25 of the Draft Articles reflects customary law at the international level in general, whereupon international investment law not may change its content single-handedly. Thus, the fact that proportionality not is the preferred standard of review in this context stands perhaps somewhat apart, as a special case scenario, from the question of diffusion of proportionality as such within international investment law. Too much reliance should, in other words, not be put on an argument discounting proportionality's potential in international investment law on the basis of it not being the preferred standard of review within the context of the customary necessity defence.

In total, proportionality is being utilized in some important investment law balancing situations (NPM clauses and indirect expropriations), but not in others (fair and equitable treatment). Relative to only a few years back (before *Continental Casualty* and *Tecmed*), its significance has increased. A conclusion might thus be that proportionality currently holds

a sectorial dominance as the preferred standard of review in some considerable parts of international investment law, and that its sphere of influence is expanding. If this trend continues, proportionality might very well end up being adopted on a general basis by investment tribunals within a decade or two, tribunals who thereby would follow the in wake of the ECJ and European Court of Human Rights.³⁷⁴

6.2 The utility of proportionality

As was briefly discussed in section 1.1, the economical importance of international investment law is on the rise both in absolute and relative terms. There are indications that the recent international credit crisis may boost this effect: Foreign investors have been treated discriminatory relative to national investors in terms of gaining advantages from the emergency measures implemented to counteract the crisis (so-called “national treatment”),³⁷⁵ and those covered by BITs, MITs or investment contracts that prohibit such treatment may very well choose to initiate arbitral proceedings against the host states in question on the basis of the latter breaching said legal instruments. The investors may also assert that this conduct constituted a breach of the fair and equitable treatment standard. As the states typically may take the path of Argentina in defending their measures by way of NPM provisions and/or the customary necessity defence, balancing may become an (even more) essential part of arbitration practice in the years to come: As seen in chapter 5; the evaluation of NPM clauses, the customary necessity defence and the fair and equitable treatment standard all require the tribunal to conduct a weighting of opposing norms interests and values, and thereby the question of which standard of review it is to utilize when conducting those operations will possibly be allocated considerable attention.

Proportionality may hereunder not only be considered as a standard of review choice currently holding some actual merits, but also as a best-practice alternative. It represents a

³⁷⁴ See sections 3.2.1 and 3.2.2.

³⁷⁵ See Van Aaken, A. and Kurtz, J., *The Global Financial Crisis: Will State Emergency Measures Trigger International Investment Disputes?* and Calamita, N. J., *The British Bank Nationalizations: An International Law Perspective*.

unique procedural framework for several reasons: First of all, among the alternatives presented in this thesis (which, as seen, are the ones presently accounted for in an international legal context), proportionality is the only one that explicitly incorporates both a weighting of the state measure relative to alternative measures the state could have implemented (necessity), and a weighting of the state measure relative to the importance of the opposing norms interests and values (proportionality *stricto sensu*). It is arguable that both of these steps are required to achieve reasonable legal results under all conditions: If the necessity stage is thought away, the state would be justified in implementing any measure regardless of whether less restrictive equally effective alternatives existed. If the proportionality *stricto sensu* stage is thought away, the state would be justified in implementing any measure however disproportionate in relation to the investor's interests. While tribunals, such as the WTO Appellate Body, from time to time have jumbled the steps together into a combined, somewhat opaque, assessment,³⁷⁶ a standard of review that embraces them both through a formal framework must be considered the better alternative in terms of juridical predictability and consistency.

Second, proportionality injects 'a measure of analytic, or procedural, determinacy to the balancing exercise'³⁷⁷: Balancing has, as seen, been criticized for legitimizing juridical law-making, thereby allowing a tribunal to dabble in complex value-laden and empirical issues best left for elected representatives, and possibly undermine the state's legislative authority. Such fears, however, may be mitigated by a clear, predictable and consequent balancing process under which the tribunal is bound by a methodological framework to assess the crucial component parts of the weighting of the opposing interests in a nested sequence of logical steps. Thereby, the feared collapse of the process into an *ex aequo et bono* assessment may be contained at the procedural level. As shown just above, proportionality represents the only balancing framework that explicitly takes into account all the intrinsic component parts of the balancing process. Furthermore, it is a wide-ranging method of analysis, usable under more or less any thinkable scenario. It thus represents the best-practice alternative along this axis.

³⁷⁶ See sections 3.1.2 and 5.1.2.

³⁷⁷ Sweet, A. S., *Investor-State Arbitration: Proportionality's New Frontier* part III section B page 63.

Third, proportionality may also help legitimize the arbitration process. An inherent strain on the latter is that while it on the one hand is entirely dependent on the consent of the parties, and thus on the perception that it is neutral *vis-à-vis* the dispute, it on the other hand is forced to declare a winner and a loser and thereby possibly erode that perception.³⁷⁸ If utilizing the proportionality framework, however, the tribunal has the opportunity to pay respect to the relative positions of both parties throughout the balancing procedure, and thereby alleviate the possible distress of the eventual loser. It forces the tribunal to do this explicitly and also promotes predictability by indicating to the parties the type and sequence of the arguments they have to make in order to cover the path the tribunal will take through its assessment.

Fourth, as seen in section 3.2, the current diffusion of proportionality is considerable both in a national and international context. By endorsing of its prospects, international investment law would thus join forces with a host of likeminded juridical subject areas.³⁷⁹ It might be argued that such confluence may constitute certain scale advantages in terms of general juridical predictability, consistency and development.

Returning finally to Xanadu and the RDA, it is presumable that the tribunal will apply proportionality only to its assessment of the NPM defence. The interpretations of the US-Xanadu BIT and the Draft Articles of State Responsibility currently do not support a more excessive utilization of the method. If one general, underlying trend was to be accentuated on the basis of the analysis in which the Xanadu case has been used as illustrative material however, it would be its prevalent emphasise on principles as opposed to rules: The discussion on the juridical topography of international investment law that both commentators and practitioners presently seem to be committed to definitely appears to be principle-based. An application of principles in turn leads to balancing, balancing requires a method, and the most advantageous method is, for the reasons just discussed, proportionality.

³⁷⁸ See Sweet, A. S. and Mathews, J., *Proportionality Balancing and Global Constitutionalism* part 2 section A.

³⁷⁹ See Franck, T. M., *Proportionality in International Law* part VII.

List of abbreviations

ASEAN	-	Association of Southeast Asian Nations
BIT	-	Bilateral Investment Treaty
ECHR	-	European Convention on Human Rights
EC	-	European Community
ECJ	-	European Court of Justice
ETC	-	Energy Charter Treaty
FDI	-	Foreign Direct Investment
FIPA	-	Foreign Investment Promotion and Protection Agreement
GATS	-	General Agreement on Trade in Services
GATT	-	General Agreement on Tariffs and Trade
GDP	-	Gross Domestic Product
ICJ	-	International Court of Justice
ICSID	-	International Centre for Settlement of Investment Disputes
IMF	-	International Monetary Fond
ILC	-	International Law Commission
LDC	-	Less Developed Country
MAI	-	Multilateral Agreement on Investment
MFN	-	Most Favoured Nation
MIT	-	Multilateral Investment Treaty
NPM	-	Non-Precluding Measure
NAFTA	-	North American Free Trade Agreement
OECD	-	Organization for Economic Co-operation and Development
PCIJ	-	Permanent Court of International Justice
UNCTAD	-	United Nations Conference on Trade and Development
WTO	-	World Trade Organization

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